International Labour Conference
85th Session 1997

Report V (1)

# General conditions to stimulate job creation in small and medium-sized enterprises

International Labour Office Geneva

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# CHAPTER I

# INTRODUCTION

## 1. Background to the topic in the context of the ILO

At its 262nd Session in March 1995 the Governing Body selected the topic "General conditions to stimulate job-creation in small and medium-sized enterprises" for inclusion in the agenda of the 1997 Session of the International Labour Conference with a view to adopting an instrument.

The last comprehensive discussion on small and medium-sized enterprises (SMEs) in the ILO took place at the 72nd Session of the International Labour Conference in 1986, which adopted a resolution concerning the promotion of small and medium-sized enterprises (see annex). More recent discussions on the promotion of self-employment, held at the 77th Session of the Conference in 1990, provided an opportunity to review some of the issues involved in the promotion of units at the bottom end of the small and medium enterprise spectrum. The topic of SME promotion and its importance for employment generation has also been discussed at several recent regional conferences, most recently by the Eighth African Regional Conference (1994).

A number of international labour standards make direct or indirect reference to issues of employment and the role of small and medium-sized enterprises. These include:

— the Employment Policy Convention, 1964 (No. 122), and the Employment Policy (Supplementary Provisions) Recommendation, 1984 (No. 169);

— the Human Resources Development Convention, 1975 (No. 142), and the accompanying Recommendation (No. 150); and,

— the Cooperatives (Developing Countries) Recommendation, 1966 (No. 127).

## 2. Rising levels of unemployment

The last decade has seen an increasing recognition of the important role of small and medium-sized enterprises in the creation of jobs and the promotion of economic growth and development. Recent statistics from OECD countries indicate that small enterprises account for the vast majority of new jobs. There are indications that the situation is similar in many developing countries.

Although data are scarce, it is clear that this situation is even more pronounced in transition economies where large-scale restructuring, privatization and the introduction of free-market principles and other dramatic changes are creating new market opportunities and strong growth in the small and medium enterprise sector; this, despite policy, legal and regulatory environments which are often not conducive to the needs of business.

The positive performance of the small and medium enterprise sector must be seen against a global situation where employment concerns have risen to the top of the agenda in virtually every part of the world.

In most industrialized countries, unemployment has risen substantially over the past 20 years. The average level is now approximately 8 per cent in OECD countries and has reached almost 12 per cent among European Union (EU) members. Persistently high unemployment is combined with reduced employment prospects for unskilled workers and rising wage inequality between skilled and unskilled workers.

In the transition economies of Eastern and Central Europe and the Commonwealth of Independent States (CIS), there has been a dramatic increase in unemployment since 1990. Unemployment rates of over 10 per cent are now common and threaten to rise with continued economic restructuring towards a market economy. Real wages have fallen and poverty has increased in several countries in the region.

In the developing world, there has been a collapse of modern-sector employment in most of sub-Saharan Africa, with rising unemployment and substantial falls in real wages. In Latin America there was also a general deterioration in employment conditions during most of the 1980s. There, the bulk of job-creation was in low-productivity informal sector activities as a response to rising urban unemployment and falling real wages. It is only in Asia, especially in the rapidly growing countries of East and South-East Asia, that there has been sustained improvement of the employment situation (ILO, 1995a).

## 3. The changing global context and the implications for small and medium-sized enterprises

Concerns over the issue of job-creation have surfaced against a backdrop of profound changes in the global economy which are altering the environment in which small and medium-sized enterprises operate and compete. This has spurred new and innovative strategies designed to enable the sector to achieve high levels of growth and efficiency more effectively. This report will address the new challenge and review ways to stimulate employment in the small and medium enterprise sector.

The past few decades have seen steady growth in world output, international trade and direct investment flows. World output has increased by at least 3 per cent per annum since 1950. World trade has grown even faster throughout this period, and the rapidly increasing share of manufactured goods now constitutes 71 per cent of the total value of world exports. The growth of manufactured exports from developing countries has been particularly rapid and flows of direct foreign investment have increased massively in recent years.

The structure of output and employment has changed radically. There has been a significant shift from agriculture to industry and services, with agriculture now accounting for only 4 per cent of world output. Moreover, there has been significant industrialization in developing countries where the share of manufactured goods has risen to over 20 per cent, similar to that of industrialized countries where a marked shift towards services means that the services sector now accounts for nearly 65 per cent of total output. The structure of employment has changed accordingly.

Following increased liberalization and advances in communication technologies, globalization of financial, product and labour markets has accelerated. This has led to

increased competition, particularly from rapidly developing countries in East Asia and Central and Eastern Europe. Firms, increasingly engaged in global sourcing, pull even remote regions into worldwide supply networks. At the same time, all countries are becoming markets for other countries' exports. As the world economy becomes further integrated, local standards are no longer competitive and the pressure increases to reach international standards.

There have also been profound changes in the organization of production. Economies of scale have been declining as techniques such as lean manufacturing and just-in-time production have shifted the attention from size to timeliness, and computerized production has allowed smaller factories to produce customized goods at mass-production prices. The plummeting price of information technology allows small and medium-sized enterprises to compete with the giants and gives them the added edge of flexibility in information-dependent innovation. Also, there has been a rapid growth in subcontracting between large enterprises and SMEs.

Large companies have responded to intense international competition by "downsizing" and outsourcing. This has involved cutting staff, eliminating entire layers of management, contracting-out functions (such as computer services), splitting into smaller units or transferring production to lower-cost countries.

Economic globalization and decentralized business strategies have been paralleled by new supranational political configurations. And while trading blocs such as the Common Market of the Southern Cone (MERCOSUR), the North American Free Trade Agreement (NAFTA) and the EU take on new economic functions within nation States, many policy initiatives are being conceived and implemented locally.

Many of these changes profoundly affect the context in which enterprises, including small and medium-sized enterprises, have to compete. It is becoming ever more important for small and medium-sized enterprises to remain flexible and competitive by upgrading quality and productivity and keeping costs low. These new pressures have led many countries to conduct a fundamental reappraisal of the small and medium enterprise sector in the light of existing policies. Innovative ways are emerging of gaining competitive advantage.

## 4. The report

This report is concerned with policies, strategies and programmes for the creation of sustainable and productive jobs in small and medium-sized enterprises. Underlying the report is a basic concern with both the quantitative and qualitative aspects of this employment. Good working conditions, security and fairness cannot be treated as separate from, or additional to, small and medium enterprise development but should rather be an integral part of a wider strategy to promote efficient and competitive small and medium-sized enterprises.

Chapter II of the report reviews the general characteristics, potential and problems of the small and medium enterprise sector, provides an overview of recent employment trends in small and medium-sized enterprises and reviews data on qualitative aspects of small and medium enterprise employment, including working conditions, safety and health and terms of employment.

Chapter III summarizes international experiences to date in creating an enabling environment for small and medium enterprise growth and development. The major

policy areas are looked at from an SME development perspective and legal and regulatory constraints are examined. This section reviews experiences with structures and processes which have helped create and maintain a favourable environment for the growth of small and medium-sized enterprises.

Chapter IV analyses the services, institutions and programmes which support the emergence of a competitive and growing small and medium enterprise sector to generate productive and sustainable jobs and proposes strategies which are relevant, cost-effective and sustainable.

Chapter V provides an overview of international labour standards as they apply to the SME sector.

Chapter VI surveys the roles of governments, employers' and workers' organizations and other actors in small and medium enterprise promotion.

## CHAPTER II

# GENERAL CHARACTERISTICS, POTENTIAL AND PROBLEMS OF SMALL AND MEDIUM-SIZED ENTERPRISES

### 1. Definition of small and medium-sized enterprises

No single definition can capture all the dimensions of "small" or "medium" business size, nor can it expect to reflect the differences between firms, sectors or countries at different levels of development. Small and medium-sized enterprises (SMEs) have historically been defined against various criteria, including:

— the number of persons employed;
— the volume of output or sales;
— the value of assets employed; and,
— the use of energy.

Other definitions stress qualitative aspects such as whether the owner of the enterprise works alongside workers, and the degree of specialization in management (ILO, 1961); and whether or not an enterprise lies in the "formal" sector. Whatever criteria are used, inadequate classification is inevitable. For instance, a highly capitalized, or technologically sophisticated enterprise might employ few people. A small food processing unit may use a large number of employees during the harvest season. Or a labour-intensive unit might have a precarious economic base. Moreover, the significance of the criteria may vary according to whether the promotion or protection of SMEs, the application of labour legislation or other special measures are under consideration. Typically, a firm located in the informal sector is thought of as a very small-scale operation, family owned and operated, and characterized as unregulated and unprotected, and outside mainstream policies and institutions, such as the tax, health-care and training systems. Different measurements of size are useful for particular needs — for instance, the asset value for purposes of financial review. In practice, the numbers of persons employed is probably the most common criterion, and it is the one that has been mainly adopted in this report.

The OECD defines establishments with up to 19 employees as "very small"; with up to 99 as "small"; from 100 to 499 as "medium"; and with over 500 as "large". However, many establishments falling into the OECD's medium-size category would be regarded as relatively large firms in some developing countries, so that the definition can be expected to vary greatly according to national conditions.

Small business is closely linked to the practice of entrepreneurship. An entrepreneur can be defined as one who surveys the potential of his business environment, identifies opportunities to improve it, marshals resources, and acts to maximize operational opportunities. The term includes those in large, medium and small enterprises as well as in cooperatives and government; it can even be used in

**Table 2.1. Distribution of employment by enterprise size: Industry and market services (percentages)**

| Country | Year | Very small | Small | Total small | Medium | Large | Total |
|---|---|---|---|---|---|---|---|
| | | 1-19 employees | 20-99 employees | 1-99 employees | 100-499 employees | 500+ employees | |
| Australia | 1992 | 36.6 [1] | 22.6 | 59.2 | 40.8 [2] | . . . [3] | 100 |
| Belgium | 1991 | 25.2 | 20.8 | 46.0 | 19.1 | 34.9 | 100 |
| Canada | 1991 | 27.2 | 22.3 | 49.5 | 15.9 | 34.6 | 100 |
| Denmark | 1991 | 38.4 | 23.0 | 61.4 | 17.6 | 21.0 | 100 |
| Finland | 1989 | 26.3 [1] | 18.0 | 44.3 | 17.1 | 38.6 | 100 |
| France | 1990 | 29.1 | 21.0 | 50.1 | 16.2 | 33.7 | 100 |
| Germany | 1990 | 25.9 | 18.7 | 44.6 | 18.2 | 37.2 | 100 |
| Italy | 1988 | 58.2 [1] | 13.2 | 71.4 | 9.9 | 18.7 | 100 |
| Japan | 1992 | 36.4 [4] | 17.7 [4] | 54.1 | 18.3 | 27.6 | 100 |
| Luxembourg | 1991 | 25.3 | 24.7 | 50.0 | 26.6 | 23.4 | 100 |
| Portugal | 1991 | 34.6 | 25.0 | 59.5 | 19.5 | 21.0 | 100 |
| Spain | 1991 | 42.4 | 23.0 | 65.4 | 14.5 | 20.0 | 100 |
| Sweden | 1988 | 24.4 | . . . [3] | . . . [3] | . . . [3] | . . . [3] | 100 |
| Switzerland | 1991 | 32.5 | 22.0 | 54.5 | 20.1 | 25.4 | 100 |
| United Kingdom | 1991 | 33.0 [1] | 16.1 | 49.1 | 17.2 | 33.8 | 100 |
| United States | 1991 | 24.6 | 18.8 | 43.4 | 13.5 | 43.1 | 100 |

[1] 0-19 employees. [2] 100+ employees. [3] Data not available for reasons of confidentiality. [4] 1-29 and 3-99 employees.
Source: OECD: *Employment Outlook*, 1994 (table 3.11, p. 124).

non-work situations, for instance for a person who improves social and economic conditions in the local community.

This report is concerned essentially with the role of the entrepreneur, of government and of the social partners in relation to SMEs. It looks at how SMEs have evolved, including modern enterprises in the formal sector with no more than 100 workers, family businesses engaging three or four family members, cottage industry, artisanal enterprises, micro-enterprises and self-employed workers in the informal sector of the economy. It covers all types of ownership, including limited liability companies, partnerships, cooperatives, and sole ownership. The report considers manufacturing businesses engaged in small-scale building and road construction, transportation, maintenance and repair services, trade, and professional services, but excludes agricultural production in the form of farming. It takes account of "micro-enterprises" (a term widely adopted in recent years in preference to "the informal sector" so as not to prejudge the sector's varied characteristics). Generally, the scope of the report extends to all enterprises where the major operational and administrative management decisions normally rest with one or two people.

**Table 2.2. Distribution of enterprises and employment by sector in the European Union (12 countries), 1990**

| Sector | No. of enterprises ('000s) | Micro | Small | Medium | Large | Total employment (millions) |
|---|---|---|---|---|---|---|
| | | 0-9 employees (%) | 10-99 employees (%) | 100-499 employees (%) | 500+ employees (%) | |
| Extraction | 150 | 7 | 17 | 15 | 61 | 4.3 |
| Manufacturing | 1 750 | 15 | 28 | 21 | 37 | 27.4 |
| Construction | 1 890 | 44 | 34 | 11 | 10 | 8.8 |
| Wholesale trade | 1 510 | 34 | 35 | 22 | 9 | 7.6 |
| Retail trade | 3 530 | 58 | 20 | 9 | 14 | 12.1 |
| Transport/communications | 910 | 19 | 16 | 9 | 56 | 7.1 |
| Producer services | 1 830 | 28 | 20 | 15 | 37 | 11.3 |
| Personal services | 4 210 | 49 | 23 | 13 | 15 | 15.8 |
| Total | 15 780 | 32 | 25 | 15 | 28 | 94.6 |

Source: ENSR: *The European observatory for SMEs* (Zoetermeer, Netherlands, EIM, 1994).

## 2. Employment in small and medium-sized enterprises: An overall perspective

### *Industrialized countries*

#### *Distribution of private non-agricultural employment*

Small and medium-sized enterprises are major contributors to private sector employment in the industrialized countries. According to the OECD (1994), SME employment in member countries accounts for between 57 per cent (United States) and 81 per cent (Italy) of employment in industry and market services combined. The share of small enterprises alone ranges from 44 per cent (Canada) to 71 per cent (Italy). A detailed breakdown by country is shown in table 2.1.

#### *Sectoral distribution*

The 12 countries of the EU had 15.8 million non-agricultural private enterprises in 1990. Of these, 14.7 million were micro-enterprises, almost 1 million were small, approximately 70,000 had between 100 and 500 employees and only 13,000 employed more than 500. Micro-enterprises accounted for 31.8 per cent of total employment in private enterprises outside the agricultural sector, small enterprises for 24.9 per cent and medium-scale enterprises for 15.1 per cent. Distribution by economic sector is shown in table 2.2.

#### *Small and medium-sized enterprises in manufacturing*

Small and medium-sized enterprises remain important players in manufacturing activities, even in countries with advanced industrial sectors (see table 2.3).

**Table 2.3. Percentage distribution of employment and value added in the manufacturing industry in Germany, France and Italy, 1987**

| Size and class of enterprise | Employment | | | Value added | | |
|---|---|---|---|---|---|---|
| | Germany | France | Italy | Germany | France | Italy |
| Small (20-99) | 14.6 | 23.6 | 33.7 | 12.1 | 19.0 | 29.9 |
| Medium (100-499) | 24.8 | 26.4 | 28.5 | 22.6 | 23.9 | 28.9 |
| Large (500+) | 60.1 | 50.0 | 37.7 | 64.8 | 57.1 | 41.2 |
| Total | 100 | 100 | 100 | 100 | 100 | 100 |

Source: EUROSTAT: *Structure and activity of industry, 1985/1986* and *1986/1987* (Brussels, 1989 and 1990).

## *Developing countries*

### *Distribution of private non-agricultural employment*

Information about the size and distribution of employment in non-agricultural activities in developing countries is sketchy. In the Asia and Pacific region a recent survey of 17 economies conducted for the Asian-Pacific Economic Cooperation forum (APEC) found that the percentage of the workforce in small and medium-sized enterprises varied from 32 per cent in the Philippines to 84 per cent in China (see table 2.4). The survey also found, however, wide differences in the definition of what small and medium-sized businesses actually are. Indicators included:

— number of employees;
— amount of invested capital;
— total assets;
— turnover and production capacity.

Moreover, many of the figures exclude micro-enterprises and rural-based companies for which statistics are not available on a countrywide basis.

Up-to-date information on the contribution of small and medium-sized enterprises to job creation in Latin America is scarce. The latest estimates for Latin America indicate that SMEs are responsible for between 36 per cent (Colombia) and 79 per cent (Brazil) of non-agricultural employment (Späth, 1993).

For Africa a recent ILO report estimated that 61 per cent of the labour force outside agriculture is employed in micro-enterprises and 21 per cent in the modern sector, including private enterprises and the public sector, with the remaining 18 per cent being unemployed (ILO, 1994).

## *Transition economies*

In the past, in Eastern Europe and the countries of the former USSR, central planning and state ownership resulted in industrial structures dominated by large enterprises. For example, at the end of 1991 in the Russian Federation, there were over

**Table 2.4. APEC members' workforce in small and medium-sized enterprises**

| Country/area | Workforce percentage |
|---|---|
| Australia | 39.6 |
| Brunei Darussalam | 69.4 |
| Canada | 59.2 |
| China | 84.3 |
| Hong Kong | 63.0 |
| Indonesia | 79.2 |
| Korea, Rep. of | 78.5 |
| Malaysia | ... |
| Mexico | 50.8 |
| New Zealand | ... |
| Philippines | 32.0 |
| Singapore | 44.0 |
| Thailand | 73.8 |
| United States | 53.7 |
| Taiwan, China | 68.6 |

Source: APEC, cited in "Small, medium-sized firms reveal major differences", in *Bangkok Post*, 27 Oct. 1994.

2,800 large enterprises with over 1,000 workers in the civilian manufacturing sector (excluding the military-industrial complex). One hundred and thirteen of these were very large, with over 10,000 workers. Smaller enterprises with fewer than 200 workers were responsible for less than 7 per cent of the total employment in civilian manufacturing. However, the transition to a market economy is encouraging the establishment of new private enterprises, mostly starting their operations on a small scale. Also, privatization programmes can be expected in many cases to lead to the break-up of large state monopolies and the emergence of large numbers of smaller companies.

In Poland official statistics reported the existence of 2.1 million enterprises in 1995, of which 92 per cent employ five or fewer workers, 6 per cent employ six to 50, and only 2 per cent employ over 50. Small and medium-sized enterprises currently employ about 60 per cent of the workforce. There are thought to be many more small enterprises that are not officially recorded (Hübner, 1995). For the Czech Republic, by 1994 an estimated 57 per cent of all enterprises were private SMEs (Paukert, 1995).

## 3. Recent changes in the structure of employment

### *The growing significance of small firms in job creation*

While the data provide a static overview of the size and composition of the SME sector, significant shifts in employment patterns have also occurred in recent years, and the role of SMEs in net job creation has been the subject of much interest.

After many years when the share of employment in small firms appeared to be declining, recent empirical studies in industrialized countries have questioned the

inevitability of eventual employment dominance by large-scale enterprises. Data from the United States show that 66 per cent of the increase in employment between 1969 and 1975 was in firms with fewer than 20 workers, and fully 82 per cent of the increase occurred in firms with fewer than 100 workers (Birch, 1979). Also, small firms have been a major source of job creation in the United Kingdom (Doyle and Gallagher, 1987; Daly et al., 1991). Findings suggest that from 1985 to 1989 net job generation (births minus deaths plus *in situ* change) was two to three times faster in small firms (one to 99 workers) than in those with more than 1,000 employees.

The claim that small firms are greater job generators has been contested, in relation both to survey methodology and statistical accuracy (see, for example, Atkinson and Storey, 1994) and because "small" size as such may be a less significant factor than the shift towards services, where establishment size tends to be smaller. Also, much of the so-called shift to small firms may in reality be a shift to smaller establishments still under the ownership or control of decentralizing large firms.

Furthermore, although many new jobs are found in "independent" small firms, much of the growth can be attributed to the direct transfer of activities from large firms, which are downsizing, decentralizing, outsourcing and subcontracting.

Finally, the usefulness of focusing exclusively on the size of business units has been questioned (Sengenberger, et al., 1990). Economic performance may depend less on size *per se* than on organizational structures, and the public and private policies which influence the development of firms. Therefore, relations between firms, including the potential synergies between large and small enterprises, and relations between firms and supporting institutions, are also perceived as important determinants of commercial success.

Despite these ambiguities a recent OECD paper written for an OECD high-level Workshop on SMEs: Employment, Innovation and Growth concludes that the wealth of consistent information would suggest that it is extremely unlikely that substantial evidence will be developed to indicate that SMEs do not provide a major share of jobs and net job gains.

### *Recent trends in industrialized countries*

Recent statistics indicate that SMEs are indeed the major contributors to the creation of new jobs. Table 2.5 below summarizes the available evidence on the net employment change by establishment size in eight OECD member countries over the period from 1983 to 1992. In all countries, small establishments display much more rapid net employment growth than large ones. In fact, small establishments account for most of the net employment growth over the period: in Canada, Denmark and Sweden, growth in these establishments surpassed overall net job growth. Also, the performance of very small establishments seems impressive in comparison with all other sizes: in Finland, Italy, New Zealand and Sweden, this is the only type of enterprise showing employment gains.

The data in table 2.5 thus suggest that the decline in the share of small firms in the total employment in industrialized countries has been arrested, if not reversed. This conclusion is supported by a recent analysis of United States census data, which shows that the smallest firms created virtually all the new jobs in the United States between 1989 and 1991 (SBA, 1994).

**Table 2.5. Net employment change by establishment size class (annual average rates as a percentage of total employment)**

| Country | Years | Total | 1-19 | 20-99 | 1-99 | 100-499 | 500+ |
|---|---|---|---|---|---|---|---|
| Canada [1] | 1983-91 | 2.6 | 2.2 | 0.6 | 2.8 | 0.1 | - 0.3 |
| Denmark | 1983-89 | 2.2 | 2.3 | 0.3 | 2.6 | - 0.4 [2] | . . . |
| Finland | 1986-91 | - 1.6 | 0.9 | - 0.7 | 0.2 | - 1.1 | - 0.7 |
| France [3] | 1987-92 | 0.9 | 0.4 | 0.4 | 0.8 | 0.3 | - 0.2 |
| Italy [1, 4] | 1984-92 | 1.3 | 1.5 | - 0.2 | 1.3 | - 0.2 | - 0.5 |
| New Zealand | 1987-92 | - 4.1 | 0.4 | - 1.9 | - 1.5 | - 1.5 | - 1.1 |
| Sweden | 1985-91 | 1.3 | 2.6 | - 0.2 | 2.4 | - 0.5 | - 0.6 |
| United Kingdom [1] | 1987-91 | 2.7 | 1.6 | 0.4 | 2.0 | 0.3 | 0.4 |

[1] Data refers to firms. [2] 100 or more. [3] Data by establishment size class are not available for the period 1984-87. [4] Sum of size categories does not equal total as firms temporarily operating with zero employees are not classified according to size for the period 1986 to 1992.
Source: OECD: *Employment Outlook* (Paris, July 1994), table 3.12, p. 125.

### *Trends in the developing economies*

There is also evidence that small firms have made a comeback in other parts of the world. In the Republic of Korea, for example, the share of manufacturing firms in the five to 199 employee size group had fallen from 66.4 per cent in 1963 to 38.1 per cent in 1978. Over the next ten years the share of these small and medium-sized enterprises increased to 51.1 per cent (Kim and Nugent, 1994).

In Singapore small enterprises (one to 99 employees) accounted for 35.1 per cent of jobs in manufacturing in the mid-1980s compared with 29.0 per cent in the mid-1970s. In Hong Kong the share of small enterprises rose from 52.0 per cent to 59.3 per cent over the same period (Berry and Levy, 1994).

However, this pattern was not followed in all Asian countries. In the Philippines the contribution of firms in the 10 to 99 employee size bracket to total manufacturing employment declined sharply from 46.6 per cent in 1973 to 18.1 per cent in 1986.

In Colombia noticeable shifts in the structure of industrial employment have taken place since the 1950s. In the 1950s and 1960s growth was fastest among the larger firms and plants. However, during the 1970s small and medium-sized enterprise employment grew rapidly both in the aggregate and at the firm level, reversing the pattern of the previous two decades. During the difficult 1980s there was an absolute decline in employment in plants of 200 workers or more, almost no change in those with 50 to 199, and some increase in the smaller ones of ten to 49 workers.

The ILO has recently reported that micro-enterprises in Africa constitute a huge and growing source of employment (ILO, 1994). In Kenya it is estimated that employment in small-scale enterprises (including the urban informal sector) rose more than threefold from 1981 to 1991. Expansion of employment in small enterprises has absorbed over 40 per cent of the increase in the labour force in five countries of southern and eastern Africa, i.e. Botswana, Kenya, Malawi, Swaziland and Zimbabwe. Most of this increase has come from the start-up of new enterprises. Most existing businesses did not grow (Mead, 1994). The very small number of small

modern enterprises in many African countries has been referred to as "the missing middle".

*Trends in transition economies*

A restructuring process is under way in transition economies. In the Russian Federation, for example, by March 1994 some 8,500 state enterprises had passed through a voucher auction process for the transfer of ownership to managers, employees and outside private groups and individuals. These enterprises employed about 40 per cent of Russia's industrial labour force. Additionally, approximately 80,000 small-scale entities (mostly retail and service establishments with up to 200 employees) had been sold by early 1994. The private sector's share of industrial employment had reached 20 per cent and is growing rapidly (World Bank, 1994).

For the Czech Republic, between 1993 and 1994, state and local government enterprises declined from 54 per cent of all enterprises providing 84 per cent of all employment, to 22 per cent of all enterprises providing 42 per cent of jobs. Conversely, over the same period, private SMEs rose from providing 31 per cent of all enterprises to providing 57 per cent, and from providing 9 per cent of all jobs to providing 34 per cent (Paukert, 1995).

In Mongolia the private sector accounted for approximately 44 per cent of total employment in 1992. Firms with more than 50 workers were still responsible for more than 80 per cent of private employment, as the privatization of state-owned enterprises had little impact on the size of production units, particularly in industry. The majority of private sector entities, i.e. small firms with less than five workers, provided jobs for only 7 per cent of the labour force. The majority of these private entities are small businesses, retail shops, trading companies, and a scattering of manufacturing firms producing labour-intensive goods.

*The contribution of SMEs to export development*

SMEs make a significant contribution to exports. In the developed countries where data on exports by size of company are available (i.e. France, Italy, the Netherlands and Norway) SMEs account for over 30 per cent of exports. In France (all sectors) and Italy (manufacturing) SMEs export almost as much as large firms. In Turkey, they account for 62 per cent. In Italy SMEs in industrial districts are major exporters. As for Japanese SMEs, there has recently been a decline, probably due to the appreciation of the yen. Although the share of SMEs in total exports is still small in the developed countries, the rate of growth of their exports is higher than that of large firms.

In the developing countries for which data is available, the share of total exports earnings seems to be higher. In the Republic of Korea, for example, the export share of SMEs is 40 per cent, while in China they account for 50 per cent. For the developing countries of East Asia as a whole, it is estimated that SME exports account for about 40 per cent of total exports, twice the OECD rate for SMEs. Further, the rate of growth of SME exports is higher than the growth of total exports (UNCTAD, 1995b) . The share of exports by SMEs would further increase if the statistics were to include that part of the exports of large enterprises that are subcontracted to SMEs (e.g. garment exports).

## 4. Qualitative aspects of employment generation by small and medium-sized enterprises

### *Advantages of small and medium-sized enterprises*

There are many reasons, apart from the direct contribution to employment, why small enterprise promotion can be an attractive policy option. For example:

- SMEs often require less capital investment per worker than their larger counterparts. Their labour-intensive character is compatible with the relative abundance of labour, and with the shortages of capital and foreign exchange that are characteristic of developing economies;
- SMEs are effective mobilizers of local human and material resources. They can, for instance, mobilize the small savings of proprietors who would not use the banking system but will invest in their own firms. Experience in Indonesia shows that owners have a high propensity to save and invest, even at quite low income levels. Also, SMEs can often utilize scattered local raw materials that might otherwise be neglected (Marsden, 1982);
- SMEs can in many developing countries constitute a more appropriate scale of production, especially in rural areas and small townships where markets might be limited and products might be made to order;
- SMEs improve forward and backward linkages among social and economic activities of the economy;
- SMEs promote exports and hence foreign exchange earnings;
- SMEs allow more people to gain their livelihood than do large-scale firms and can help spread opportunity, knowledge and skills in the community. SME development programmes can provide opportunities to a wider range of potential entrepreneurs, who might otherwise lack the necessary skills and resources. For many women and low-income and minority groups, starting one's own small business provides an economic option previously not available. Motivation for most enterprise programmes targeted at women is to create new ways in which women can achieve self-sufficiency, on the path to economic equality (OECD, 1990);
- SMEs satisfy the demand of low-income consumers for low-cost, simple goods and services, whereas large import-substitution industries tend to produce primarily for relatively high-income consumers. Therefore, SMEs can reduce inequalities by generating income for low-income groups, and by satisfying their basic needs (Page and Steel, 1984). Furthermore, small and medium-sized enterprises can increase consumer choice by offering a greater diversity of specialized goods and services;
- SMEs are flexibly organized and, in combination with larger enterprises, provide a more adaptable economic structure by engaging in small-batch production and made-to-order or other types of "finishing" operations complementary to the activities of large-scale industry;
- SMEs act as a seed-bed and training ground for entrepreneurship and facilitate the growth of business potential to graduate to larger operations, and the development of an industrial tradition. At the same time, SMEs conserve scarce managerial abilities through less complex organization of production (IFC, 1993);

— SMEs often innovate, especially in new technologies such as micro-electronics, new materials and biotechnology, where they tend to be in the vanguard;
— SMEs provide the possibility for richer personal relations than often is possible in large enterprises;
— SMEs are often owned by residents of a community: increased local ownership means that control of economic decisions rests with people who have a strong stake in the community, resulting in greater stability of employment, more jobs for local residents and more profits being reinvested in the community;
— SMEs constitute a "labour sponge" during periods of structural adjustment.

*Problems of SMEs: Productivity and working and employment conditions*

The performance of small enterprises, whether in terms of efficiency, working conditions or degree of social protection, is mixed. In many countries there are small and medium-sized enterprises that are profitable and productive, and which provide good working conditions and wages, but in other parts of the world, particularly in some developing countries, productivity, efficiency, wage levels and social standards are in many cases unacceptably low.

For example, in respect of productivity, data for the European Community in 1988 indicate that average labour productivity tends to be lower in sectors dominated by micro, small and medium-sized enterprises. Taking labour productivity in all sectors as 100, average productivity ranged from lows of 77 in the SME-dominant sectors of construction, and 79 in micro-dominant sectors of trade, to highs of 155 and 292 respectively in the service and extraction industries dominated by large-scale enterprises (ENSR, 1994).

In respect of social protection (which refers to the provision of benefits to wage-earners and sometimes the self-employed in respect of various contingencies, such as old age, invalidity, death, sickness, unemployment, family size and health-care costs) a major reason why as much as 90 per cent of Africa's population is without any formal protection is that many of the self-employed and those in the informal sector are excluded from coverage. Many protection schemes simply exclude enterprises with less than a prescribed number of workers and/or ignore earnings below a certain limit. Another reason is that the level of compliance with social security regulations among smaller firms is low.

Reviews of existing evidence from industrialized countries indicate that incomes, working conditions and access to social protection schemes providing pension rights and health-care facilities tend to deteriorate with size (see, for example, ENSR, 1993; Storey, 1994). This was also found in a recent ILO study (see table 2.6) (Sengenberger et al., 1990). Surveys in Germany (Wagner, 1995) indicated that, compared to large enterprises, SMEs on average provide less attractive jobs in terms of wages, fringe benefits, job security, institutionalized mechanisms for workers' participation in decision-making, opportunities for skill enhancement and career development.

As to developing countries, an analysis of Brazilian census data found that average wages rose steeply up the size brackets. Expressed as a percentage of average wages in the largest firms (500+ workers), in 1985 average wages were 37 per cent in micro-enterprises (one to 19), 62 per cent in small firms (20 to 99) and 80 per cent in medium-scale firms (100 to 499) (Späth, 1993). A review of conditions in the

**Table 2.6. Average wages by enterprise [1] size, as a percentage of wages in largest enterprises**

| Country | Year | 500+ | 100-499 | 10-99 |
|---|---|---|---|---|
| France [2] | 1978 | 100 | 86.3 | 82.9 |
| Germany, Fed. Rep. of [3] | 1978 | 100 | 92.2 | 89.7 |
| Italy [5] | 1978 | 100 | 92.7 | 85.4 |
| Japan [4] | 1984 | 100 | 83.4 | 70.0 |
| United States [6] | 1983 | 100 | 73.8 | 57.0 |

[1] Italy, Germany and the United States refer to establishments. [2] Hourly pay, manual manufacturing workers. [3] Hourly pay, male manufacturing workers. [4] 30 to 99 employees. [5] Average monthly cash earnings of regular employees in all industries except services. [6] Usual weekly earnings for wage and salary earners in private non-agricultural sector.

Source: W. Sengenberger, G. W. Loveman and M. J. Piore (eds.): *The re-emergence of small enterprises: Industrial restructuring in industrialized countries* (Geneva, IILS, 1990).

manufacturing industry in Colombia confirmed the aggregate picture of better wages, fringe benefits, security and opportunities in large firms; however, it also found "enormous" differences in wage levels and non-wage benefits between large firms and small establishments, both within the same sectors and between different sectors (Dombois, 1993).

Child labour is a phenomenon that is on the increase with an estimated 100 million children worldwide having to work, of which 95 per cent are in developing countries. The increase can be seen, mostly, in the informal sector (Neck, 1993).

### *A mixed picture*

Sometimes, differences in incomes, working conditions and access to social protection can appear large. However, the average picture can hide many variations. Closer examination frequently reveals significant variations within sectors, between sectors and between geographical areas (Pyke, 1995). There are also indications that the generally inferior employment conditions offered by SMEs can, at least in part, be compensated by non-financial advantages. Thus a survey of employees in 7,000 Japanese SMEs indicated that many consider that SMEs offer a better understanding of the importance of one's work in the company, better personal control of one's work, a higher likelihood of having one's ideas accepted, and easier workplace relations with other workers. These factors are particularly important in producer cooperatives and worker-owned enterprises, where job satisfaction is often higher. Moreover, comparisons of wage levels often do not take account of income to working owners and their families, which can be significant in small enterprises.

A sense of the complexity behind the aggregate statistics is reflected in various studies: there are few uniform sectoral patterns of enterprise size and entrepreneurial incomes. Incomes yielded by micro-enterprises vary widely, and a recent ILO study suggests that a large proportion of African micro-entrepreneurs probably earn incomes equal to, or greater than, formal sector wages. Despite this, the incomes of many are lower than those of employees in the formal sector. This is particularly the case for self-employed workers in household enterprises, self-employed women, and those on the lower rungs of petty trading, street-vending and personal services (ILO, 1993b). There are many examples of innovative small firms which pay well, just as

there are cases of larger firms providing poor working conditions. Moreover, even where small firms provide comparatively poor pay, working conditions and social protection, the situation is not static, and significant improvements can be made.

That SMEs can sometimes outperform larger enterprises with regard to working conditions is confirmed by empirical data. During the 1980s, the ILO compared 56 enterprises, in textiles and garments, food products and metalworking, in eight Asian developing countries, in relation to 50 aspects of working conditions and occupational safety and health. These included:

— working postures;
— space and work surface heights;
— career and training opportunities;
— ventilation, lighting, noise and exposure to hazards;
— canteen and welfare facilities.

The enterprises compared were of various sizes but all employed fewer than 300 people. The study found that for these enterprises certain aspects, such as provision of medical services and paid sick leave, layout of machines or workstations, incidence of heavy lifting, and problems of working time or rest periods, showed clear improvements with the growing size of the enterprise. However, in the case of other aspects such as heat and ventilation problems, lighting and other physical environmental factors, exposure to hazardous chemicals, accidental injuries due to machines and equipment and poor machine design features relating to reach, height, posture, or display, larger firms were as likely to provide bad conditions and, in some respects such as noise and dust, a little more likely to do so.

Problems of working conditions tended to be interrelated. For example, when congested work space was a problem, this was often coupled with obstructed passageways and repetitive types of work. Poor ergonomic design of workstations tended to be found in conjunction with poor housekeeping and lack of protection against various hazards. A conclusion was that working conditions and occupational safety and health problems seemed to be closely related to production problems, and that solutions to inadequate conditions could pay for themselves in better enterprise performance, and even generate substantial gains in productivity and competitiveness (Kogi, 1985).

A growing body of evidence indicates that improvements in working conditions and the environment, an equitable income distribution and the security of social protection could be key ingredients of business efficiency and competitiveness. In innovative enterprises the quality of work and products are elements of the same strategy; workers' involvement and commitment are an integral part of the functional development of the enterprise; and social efficiency and environmental efficiency go hand in hand with economic efficiency. The challenge is clear: how to promote small enterprise development which combines economic efficiency and job creation with adequate social standards, working conditions and social protection. Evidence indicates that sound policy and regulatory environments, effective service delivery systems and the creation of collaborative structures and tripartite arrangements can play important roles in achieving this objective.

# CHAPTER III

# POLICY AND REGULATORY ENVIRONMENT

## 1. An enabling environment for small and medium-sized enterprises

### *The cultural climate*

In many countries there is an institutional and social bias in favour of employment in large state or private organizations. For example, a preferential status is accorded in many African educational and social systems to careers in the public bureaucracy (Gibb, 1995). By contrast, a career in small business is widely perceived as second-best, or a stepping-stone to employment in a big organization. A recent survey in Indonesia indicated that only 5 per cent of business graduates considered entrepreneurial activities as a career option (Henriques, 1995a).

Working in, and possibly establishing, a small enterprise often enjoys little socio-cultural support either in society at large or in well-educated subgroups. Certain countries exhibit strong small-enterprise cultures where the supporting values and beliefs are widely shared in the community. Elsewhere, however, this critical factor is often missing. Increasing recognition of the essential cultural underpinning of small enterprise success means that active promotion of a cultural environment, favouring entrepreneurial attitudes, skills and aspirations and the recognition of small firms as a worthwhile workplace, is attracting interest worldwide.

### *The policy climate*

Crucial to the success of small and medium-sized enterprises and their ability to generate sustainable and productive employment is a policy and regulatory environment which enables, rather than obstructs, their development. Generally, policies and regulations should enable enterprises to be competitive without undermining the achievement of social objectives. Regulations created for one set of economic or social circumstances, or time period, can become outdated. It is therefore necessary to monitor continually the application of policies, rules and procedures and their consequences, and to adapt them as required.

Official policy can foster or hinder small and medium enterprise development. It covers such areas as monetary and fiscal policy, credit, trade and tariff regulations, land tenure, infrastructure, government procurement, information technology and education and training. Even when small enterprises are protected from discriminatory application of regulations, the high cost of compliance, in both time and money, can confer an unfair advantage on large firms. The implication for enterprise competitiveness and hence employment has prompted extensive renewed interest in reform of the regulatory environment to secure general social and legislative aims, while also providing encouragement for small enterprise growth.

It is increasingly recognized that, in the past, insufficient account was often taken of the specific needs of small enterprises. Frequently, policies and regulations were not only inadequately supportive of small and medium enterprise development but even positively restrictive. Moreover, instruments to achieve social objectives in smaller enterprises have frequently been ineffective. The recent and continuing growth of small and medium-sized enterprises as a source of employment highlights the challenge of finding ways to support SMEs while combining business efficiency and competitiveness with adequate social standards and protection.

## 2. Creating an enabling cultural climate

### *Enterprise culture*

Many means can be used to stimulate an enterprise culture and promote successful entrepreneurs as role models. In Spain an annual event is held in the most prestigious building in Valencia, where small firm entrepreneurs are ceremoniously judged and receive awards in a range of categories such as innovation and quality (Pyke, 1994). In Australia, success has been achieved with a "Live Wire" programme which identifies and rewards outstanding young entrepreneurs. After identification and selection their story is widely publicized and a prize awarded by a high-ranking government and private sector panel (Henriques, 1995a). Recently, similar approaches have been initiated in Indonesia (with assistance from the ILO) as a joint effort between local business associations and the Ministry of Manpower.

One of the most important means of introducing an enterprise culture over the long term is no doubt through changes in the education and training systems of a country. Many countries have recently started introducing entrepreneurial elements at all levels of the training and education systems to ensure that graduates are given the opportunity to acquire the knowledge, skills and attitudes associated with entrepreneurship.

### *Quality and productivity culture*

Global trade conditions today are such that enterprises and the development programmes that support them must continuously improve in pursuit of world standards of quality, productivity, functional design and service. These are achieved both within and outside the firm, the latter being true for small firms whose success depends on flexible responses to a dynamic environment.

The success of any individual small firm is inextricably related to the competence of its trading networks, the quality of the workforce and an effective regulatory environment. It is therefore necessary to stimulate a quality and productivity culture by creating an awareness of certain standards, norms of behaviour and expectations as to what should be produced and how. The consumer must learn to expect a certain level of produce quality : the entrepreneur, quality production from suppliers ; and the worker, an acceptable level of working conditions. Moreover, the raising of standards, including labour standards, can create significant economic advantages for an enterprise.

Inside enterprises there is an increasing trend to flatten internal hierarchies and rely on active participation of workers to achieve quality and improve production

practices, thereby increasing productivity and competitiveness. Good industrial relations and working conditions are important contributors towards creating an environment of cooperation and quality consciousness.

An enterprise can also reap competitive advantages from its external relations. A common expectation of certain standards means that the entrepreneur does not waste time searching for good firms, controlling quality, or ensuring excessive legal safeguards in anticipation of suppliers' failed compliance with contracts. The enterprise also becomes aware of what level of competence the market expects.

There are many ways a quality and productivity culture can be promoted and standards raised. For instance, ILO Human Development Enterprise Awards to exceptional firms have been proposed to reward initiative and create a demonstration effect like Design Awards or Export Performance Awards (Standing, 1995). Another approach seeks to integrate improvements in working conditions and competitiveness within the same technical assistance programme. This has been successfully achieved by the ILO's Work Improvements in Small Enterprises (WISE) programme (see Chapter IV), and is also currently being field-tested under the ongoing ILO interdepartmental project on the informal sector.

### *Information culture*

The ability to apply knowledge has become an important source of competitive advantage for individual enterprises, industrial sectors and regions. This is because the pace of change has increased and competitiveness now depends on capacity to adapt and innovate. Consequently, policy-makers are searching for ways to facilitate an "information culture" and encourage dissemination of knowledge among enterprises. This is particularly important for small and medium-sized enterprises which often lack resources to sustain a strong information base themselves and therefore must rely on other institutions and enterprises.

Many governments have adopted policies to encourage relations between universities, research centres and the private sector. For instance, matching funds and other incentives are provided for joint projects in areas like product development, production research, equipment design and development and use of new materials. Increasingly, reduced government funds are forcing universities and other institutions to earn income from fee-based work for industry. Institutional arrangements such as science parks (see section 4 below) can also forge links between small, knowledge-intensive enterprises and research institutions.

The emergence of an organizational culture that recognizes information as an essential resource is critical to success in the new information age. This can be encouraged in many ways. In Singapore, for example, IT 2000 aims to place the country among the first in the world with an advanced nationwide information infrastructure. It will support the networking of computers in virtually every home, office, school and factory and will facilitate the efficient flow of information in any form (text, sound, pictures, video, documents, graphics and other media) and provide access to a wide range of new infrastructural services (APO, 1994). The programme will involve extensive support to small and medium-sized enterprises wanting to introduce these new tools.

Firstly, an information-sharing culture is required that fosters rather than prevents competition. It can be vexing for small firms to pass on information, especially to

perceived competitors, but mechanisms of this type are needed, such as experience exchange groups, small and medium enterprise networks and service centres, trade associations and trade unions.

Secondly, rapid advances in technology make training a lifelong process. A major role of the government is to facilitate this process through in-service training and the promotion of a "learning culture" and "learning organizations".

Finally, the rapidly changing environment also implies that government institutions need to have rapid information feedback mechanisms to give policy and technical support to meet new needs of the small and medium enterprise sector.

## 3. Creating an enabling policy climate

### *Monetary policies and economic stability*

Entrepreneurs require a stable economic climate to formulate and execute their investment and savings plans. This should include rules governing property rights, taxation and the enforcement of contracts. These preconditions are generally present in mature market economies, but in many developing and transition economies they are a major source of uncertainty. The maintenance of a stable macroeconomic framework also calls for the control of inflation through fiscal and monetary policies and an appropriate exchange rate system.

High inflation can be a particularly serious problem for small manufacturers and traders who often do not receive immediate payment on delivery. If full payment comes several months later, its value risks being significantly eroded. More generally, most small enterprises do not have the financial resources to build up stocks, nor accounting skills to calculate real costs and set prices at a level sufficient to purchase new inputs. This results in a competitive disadvantage in comparison with larger enterprises, particularly in the manufacturing sector.

### *Fiscal policies*

The tax burden for small enterprises varies widely from country to country. It is reportedly high in French-speaking sub-Saharan countries, but less consistently so in English-speaking East Africa. Many small enterprises bear heavy tax burdens through indirect taxes, flat-rate levies and the fact that they do not qualify for exemptions enjoyed by large enterprises. Fiscal incentives to encourage the development of industries often attempt to link the value of such incentives to the level of investment, with the consequence that larger enterprises receive greater benefits. The tax structure in several Asian countries, for example, imposes a penalty on the operation of small-scale enterprises (Lim, 1992).

Governments need tax revenue. How this is generated, however, requires careful attention. Compliance by small and medium-sized enterprises often involves not only paying tax but also the incremental costs of keeping otherwise unnecessary records and understanding and applying tax laws. Compliance costs are the costs of the business owner's time, or that of his staff, plus any expenses such as accountant fees. Since these costs are fixed they are regressive by firm size, that is, more burdensome for small than for large firms (Bannock, 1995). Unnecessary tax burdens on small businesses can be particularly serious in economies in transition, because tax

administration places heavy demands upon the scarce resources of trained bookkeepers and finance staff. Another effect of burdensome taxes on small firms is that money which is paid in taxes cannot be invested in the business. This is more of a problem for small firms than it is for large organizations, as the latter generally have easier access to bank loans and other sources of investment. Furthermore, high payroll taxes or social security charges raise employment costs. This is particularly significant for small and medium-sized enterprises, which often are more labour-intensive than large firms.

At least six EU Member States have a reduced rate of corporation tax for profits below a fixed threshold. In Germany very small businesses are exempt from local business taxation, and in many countries various types of tax holidays are given to start-up businesses (Bannock, 1995).

The issue of burdensome, inflexible and unclear regulations is particularly problematic in many Central and Eastern European countries which have been slow to adjust to the needs of a market economy. Most transition economies still lack basic enabling regulations in such areas as contract law, environmental protection and safety and health. Also, the pace of change and the overlapping of different bodies of law and regulations causes confusion in the minds of entrepreneurs and officials alike. A recent mission to Uzbekistan found that an inadequate policy and regulatory environment was an obstacle to the expansion of the small and medium enterprise sector. The mission's findings are described in box 3.1.

**Box 3.1. Enterprise taxation in Uzbekistan**

Taxation legislation and the associated administrative and regulatory procedures change very often in Uzbekistan as new amendments to existing taxes are made and new forms of taxation are introduced. The result of such rapid change is twofold. Firstly, many small-business owners are unable to keep abreast of these changes. Whilst the Taxation Board publishes these details, consultation with business people confirmed that it is unlikely that most businesses have the time, access or background knowledge to understand and implement them in the way in which they are intended. The second impact of these changes is that officers of the Taxation Board are often unable to understand how these changes can be properly implemented.

These two effects create a situation where the taxation system is not completely understood by either the taxpayer or the tax assessor. This means that there is a high degree of discretion which can be exploited by tax officials and business people. This creates a situation which is conducive to corruption and bribery, and many instances of these practices have been cited during research conducted in this area.

Source: S. White and J. Petterson: *Small and medium enterprise development in Uzbekistan*, consultant's report (Geneva, ILO, 1995).

Some micro-enterprises are called upon to pay significant taxes or other financial charges. In Peru the tax burden is heavier on enterprises in the informal sector than in

the formal sector. Also, in one area of the Philippines informal sector enterprises were estimated to have contributed 41 per cent of total municipal revenue but got very little back in terms of services. In Uganda informal sector taxes, dues and licence payments averaged about 66 per cent of revenues to the cities surveyed (ILO, 1993). Contrary to what may be expected, non-registered informal sector enterprises contribute significantly to municipal revenues through both formal payments and "informal" payments to local officials.

### *Finance and credit policies*

Inadequate access to formal credit is an issue for small and medium-sized enterprises and a major obstacle to their development. The causes are to be found on both the supply and the demand sides. Many problems in small enterprise finance can be attributed to the manner in which financial resources are managed within the business. In Germany less than 30 per cent of small and medium-sized enterprises work with financial planning instruments, which leads to an excessive reliance on (expensive) short-term credit. Just over 60 per cent calculate their costs systematically. Many small-business owners are not well informed about available financial instruments and rely on self-financing even where longer-term credit instruments would be preferable. Also, small businessmen often feel personally attached to their undertakings and are reluctant to share control with outside providers of equity finance.

Compared with corporations that can raise capital on the stock market, small firms are usually undercapitalized. Comparatively, small enterprises rely much more on debt finance than large corporations; this brings with it another problem, namely the need to provide collateral for bank credit. Finding the necessary collateral can be a significant problem. In Poland, for example, real estate, a common form of collateral elsewhere, is rarely accepted for small and medium enterprise loans (GEMINI, 1994). Moreover, small enterprises have smaller financing requirements, which entail relatively higher transaction costs for banks. Banks usually prefer to deal with larger enterprises. To compensate for the relatively higher risks and costs of dealing with small enterprises, banks need to have a margin that allows them to absorb these incremental costs and risks.

Many government policies address this credit problem by providing interest rate subsidies or guarantees to lending institutions, minimizing risks, reducing transaction costs and simplifying procedures. A popular approach has been to promote credit/guarantees whereby governments and international donors provide insurance against default by small and medium-sized enterprises. These approaches have been reasonably successful in industrialized countries but less so in developing countries.

Some countries, such as India, Indonesia, the Republic of Korea, Malaysia, Pakistan and the Philippines, have intervened directly in the financial market and imposed minimum quotas on financial institutions to provide loans to small and medium-sized enterprises. Credit allocation policies by way of quotas are, however, likely to lead to distortions. Furthermore, interest rate ceilings have been found to be neither suitable for targeting small enterprises nor efficient in alleviating a market access problem. In most cases the issue is not that credit is expensive but that

transaction and opportunity costs for small entrepreneurs entail access difficulties (see boxes 3.2 and 3.3).

**Box 3.2. West Africa: The importance for SMEs of access to credit**

Experience has shown that access to credit rather than the cost of credit is the bottleneck for small-scale enterprises. This was underlined by a survey of small-scale enterprises in West Africa. Some of the small-scale entrepreneurs interviewed complained about the level of interest rates but cited, as a main problem, the lengthy and difficult procedures for obtaining credit. Many of the small entrepreneurs interviewed stated that they never had tried to apply for credit because of the high collateral requirements, bureaucratic procedures, hidden costs and the banks' lack of willingness to serve small enterprises.

Source: B. Balkenhol and C. Lecointre: *Pratiques bancaires dans les opérations de crédit avec les petites et moyennes entreprises en Afrique de l'Ouest*, Working Paper No. 7 (Geneva, Poverty-oriented Banking Programme, 1994).

**Box 3.3. Nigeria: Commercial banks supporting SMEs**

In Nigeria a relaxation of interest rate structures and credit allocations laid down by the Central Bank, together with the opening up of the banking system to more competition, has resulted in the establishment (since 1985) of large numbers of private commercial, merchant and local community banks. Interest rates have tripled and the banks have been allowed much more leeway in setting their rates. The number of Government-designated privileged lending sectors has fallen sharply. As a result, lending by commercial and merchant banks to small and medium-sized enterprises between 1985 and 1990 rose more than sixfold in absolute terms, from its previous level of 7 per cent of total commercial and merchant bank lending. Although most of the increase (80 per cent) represented diversions from other financial sectors, a substantial amount (20 per cent) reflected an increase in credit volume.

Source: ILO: "Entrepreneurship and small enterprise development in urban and rural sectors in Africa", Part 2 of the Report of the Director-General to the Eighth African Regional Conference, Mauritius, Jan. 1994.

### *Trade and tariff policies*

Import substitution strategies have tended to favour large firms at the expense of small. Trade barriers have been introduced to limit the inflow of foreign goods competing with domestic production, while overvalued currencies have aimed at reducing the costs of imported raw materials and intermediate goods needed for domestic production. As a result, domestic firms which produced the formerly imported goods enjoyed special preferences. Usually, these firms were large

enterprises producing on a capital-intensive scale. Small-scale enterprises which relied on local inputs and acted on highly competitive local markets could not profit from this trade policy. They were discriminated against because the import substitution facilitated higher wages and profits in the capital-intensive large-scale sector, rather than in the labour-intensive small-scale sector.

Furthermore, trade barriers implied quantitative restrictions through administrative measures such as import licences. Usually, small entrepreneurs did not have access to these. The resulting disadvantages are either limited access to raw materials and other imported items or dependence on prices dictated by often monopolistic retailers and trading houses. In Nepal, for example, over one in three of a survey of small entrepreneurs stated that a major constraint on the growth of their business was the limited and irregular supply of raw materials. More than half who had requested import licences reported serious problems. Among the main problems cited were lengthy administrative procedures, extra payments and rejected applications because of the small size of the firm (Meier and Pilgrim, 1994).

Items which attract high tariffs because they are perceived by the authorities basically as consumer goods may be important production inputs to small enterprises. Examples could be high tariffs on emulsion paints, fibre building boards, sewing-machines, tailors' scissors, woven fabrics and hand tools; or tariffs which make it cheaper to import finished farm implements and tools than the materials with which they can be produced locally.

In the Philippines export quota allocations, such as those used in garments, are administered in Metro Manila. The 20 per cent of the total export quota which is at present reserved for small and micro-enterprise bidding does not yet provide effective accessibility, particularly for enterprises located outside Manila. In practice, it is principally the larger enterprises which use the opportunities provided by the present semi-restricted trade system, since smaller firms cannot comply with the documentation and procedural requirements or pay the transaction costs of the system (Allal, 1995).

A comparison of the structure of effective protective rates and the size distribution of enterprises in countries of the Association of South-East Asian Nations (ASEAN) has revealed that effective protection tends to be particularly high in industries where small-enterprise shares in production are relatively low. Moreover, biases against small enterprises have been found within industries as well as between them. Due to their relative importance and easier access to influential administrators, large enterprises are likely to be more successful than smaller ones in arranging government protection against external competition (Lim, 1992).

### *Landholding policies*

A widespread problem for urban micro-enterprises is the lack of secure access to land and premises. Many micro-enterprises occupy land to which they have no legal titles or right of access. Many others pay high rents to landlords because they cannot obtain access to space or premises of their own. In French-speaking Africa a survey has reported that a very frequent cause of the closure of micro-enterprises is the demolition of the buildings in which they are located (ILO, 1994).

Complicated and expensive procedures for registering land title work against small enterprises. Zoning policies aimed at foreclosing industrial activities within

residential areas also often inadvertently work against the interests of small firms. Such firms are less likely to have the capital necessary to establish themselves in special industrial estates located far away from the small enterprise's local market. Consequently, the enforcement of zoning regulations can cause serious disruption for small firms located in non-permitted areas. In many countries relations between informal sector operators, particularly street vendors and local authorities, are often antagonistic in nature. Few municipalities attempt to accommodate them or to negotiate mutually beneficial agreements.

Public investment in premises to be leased to small enterprises can help in some situations, particularly the construction of covered public markets in which spaces can be rented and stalls erected. Simplified land title procedures and a more imaginative use of zoning policies would also help.

### *Infrastructure policies*

Infrastructure bottlenecks can be a serious constraint on any enterprise. In some countries serious problems have been caused by infrastructural inadequacies, including unreliable power supplies, poor roads, traffic congestion and inadequate telecommunications. Brownouts and other disruptions increase the cost of starting and running a business. Back-up power generation, long delays in telephone connections and frequent interruptions of production activities add further to the costs of business.

In West Africa frequent electricity failures are said to pose great problems for small enterprises which cannot afford their own generators. In East African towns up to 68 per cent of urban artisans have been found to operate in premises without either electricity or water supply (ILO, 1993). These conditions severely inhibit an enterprise's productive possibilities.

### *Government procurement policies*

In many countries intensive purchasing makes the government a major buyer of a wide range of goods and services. Generally, governments do not buy or give out tenders to any particular group of firms. However, policies often favour larger firms in the perceived interests of administrative efficiency and the search for economies in purchasing. Orders tend to be placed in relatively large amounts and often by selective tender favouring larger enterprises (Lim, 1992). There are examples — in Latin America, for example — of municipalities successfully subcontracting a range of services such as garbage collection, recycling, park maintenance and other services to associations of micro-entrepreneurs.

### *Information technology policies*

The globalization of the world economy as well as rapid developments in technology and communications have made it increasingly important for all enterprises, including small and medium-sized enterprises, to be able to benefit from developments in information technology. This extends to international E-mail networks and access to databases on technology, production processes, quality standards, fashion trends and innovations.

Within enterprises information technology has had profound implications for management information systems, accounting and administration, computer-aided design and manufacturing, decision-making, stock control and marketing. Between enterprises electronic data processing is increasingly used to connect firms with their subcontractors and manufacturers with retailers, facilitating just-in-time delivery systems and "real time" consultations on product specifications and ideas.

Many governments recognize that information technology is of critical importance in ensuring future competitiveness and productivity of enterprises. Consequently, they have adopted policies to accelerate its introduction and use. This has involved building a basic telecommunications infrastructure and promoting its use by new users, including small enterprises, through:

— training of information technology professionals;
— support for local application research;
— support for small and medium enterprise staff training;
— demonstration schemes to introduce information technology in small and medium-sized enterprises; and,
— subsidized consultancy services.

Longer-term efforts to introduce information technology at all levels of the school system and in technical training have also been important.

A country with a well-developed "informatization policy" with a strong small and medium enterprise component is Japan. Education for informatization, for example, is delivered through organizations such as the Institute of the Japan Small Business Corporation, which provides training for government advisory personnel involved in small and medium enterprise advisory services as well as for small and medium enterprise personnel and owners.

The Corporation has also established a Small and Medium Enterprise Office Automation Systems Centre which provides guidance and counselling in this area. Other policies include:

— leasing services for equipment modernization;
— financial support for informatization;
— preferential tax rates for new technology investments;
— an informatization "plaza";
— information services; and,
— standardization of business telecommunication protocols.

A National Small Business Information Centre with a network of local offices has also been established to facilitate access of small and medium-sized enterprises to databases on production, quality and other management areas.

### *Education and training policies*

The ILO's Human Resources Development Convention, 1975 (No. 142), requires that each Member adopts comprehensive vocational training policies that take due account of employment needs and opportunities. The corresponding Recommendation (No. 150) further asserts that such policies and programmes should

include self-employment among their objectives. Training should also cover all branches of economic activity including, for management, developing an adequate understanding of economic and social aspects of decision-making and, for self-employment, training in the basic principles and practices of management and developing awareness of the need to take initiatives and assess and accept risks.

In relation to new industries, the Recommendation foresees the need for independent workers and entrepreneurs to learn adequate skills to undertake subcontracting, and for supplementary training in response to changes in local economic conditions.

Growing unemployment in many parts of the world has, however, shown the limitations of the training and education systems in most countries, whether developing or developed. While the number of jobs in large enterprises and government services is stagnating, or even shrinking, education and training do not prepare graduates adequately for a labour market where most new jobs are in small and medium-sized enterprises. This has led many countries to review and reform education and training policies to reflect better the special needs of SMEs.

### *Education*

Education may be viewed as systematic instruction for the lifelong development of mind and character. The practice of providing education in small-firm entrepreneurship is growing fast, in industrialized, developing and transition economies (Gibb, 1995). Programmes for entrepreneurship recognize the concern in many societies to increase awareness of entrepreneurship as a career option. They include efforts in primary, secondary, further and higher education to develop entrepreneurial potential, understanding and motivation.

Often such programmes seek to stimulate specific segments of the population towards entrepreneurship, for example ethnic groups, the unemployed, women, inventors and scientists, second career mature managers, civil servants, retired army officers and others. The "Own Your Own Business" programme is a well-known attempt to promote entrepreneurship by television across the Canadian Province of Quebec (ILO, 1992). Norway also provides an interesting example of policies to promote entrepreneurship at every level of the general education system (see box 3.4). In Indonesia the ILO has assisted the Government in its efforts to incorporate entrepreneurial elements into tertiary business schools and vocational training institutions.

### *Training*

Training is mainly identified with a career or job. It is designed to raise the individual to a desired standard of efficiency, not by instruction only but also by the practical application of skills and knowledge. In many countries efforts are under way to increase access to training for small and medium-sized enterprises. Training programmes can:

**Box 3.4. Norway: Learning entrepreneurship**

The participation of schools in local development has become part of the Government's policy of innovation and entrepreneurship. In the primary and secondary education sectors students are encouraged to create their own "pupil enterprises". Under this scheme, students run their own enterprises, from the development of a business idea to the organization of production and the commercialization of the product. Teachers and local businessmen give advice. Enterprises in different local schools are encouraged to network and learn from one another.

In the further education sector Norwegian authorities in 1994 established resource centres in which secondary schools (with pupils aged 16 to 19) take an active part. These centres aim to bring students into closer contact with the local business environment.

Measures for increasing the entrepreneurship training in college and university education were started in 1992. The objective is to give students a better knowledge of entrepreneurship and greater motivation for and more information about starting up their own business. The aim in the future is to intensify such initiatives so that students can fully understand the problems facing entrepreneurs and the relevance of entrepreneurship to the total economy. A major objective is to motivate students to start their own business.

Source: UNCTAD: *Country presentations to the Ad Hoc Working Group on the Role of Enterprises in Development* (Geneva, 1995).

(a) deliver information on changes in the regulatory and trading environment;
(b) offer basic business techniques and systems (e.g., managing cash flow, debtor/creditor relations and producing adequate costing systems);
(c) teach negotiating, selling, persuading and other soft skills to entrepreneurs;
(d) provide opportunities to reflect on development issues, such as coping with the problems and opportunities of survival and growth (Gibb and Henriques, 1995).

Programmes can be provided by different sources, including:

— non-governmental organizations;
— state development agencies;
— local authorities;
— educational establishments;
— chambers of commerce and trade;
— management development institutions;
— business associations;
— individual consultants; and,
— autonomous small-enterprise training institutions.

Training policies for small and medium-sized enterprises must recognize and overcome a number of factors reflecting the special characteristics of the sector.

Generally the entrepreneur learns by experience, is predisposed towards practical training and mistrusts academic approaches. This is often compounded by the entrepreneur's feeling that there is no time for training and by logistical problems resulting from the heterogeneity and geographical dispersion of SMEs.

Small and medium enterprise training policies need to:

— encourage a positive attitude through promotional campaigns which emphasize the impact of operational improvement on enterprise performance and profitability;

— emphasize the training of trainers and consultants to apply pedagogical skills suited to the operational realities of SMEs;

— encourage active, flexible and practical training methodologies;

— equip the entrepreneur with adequate information to select appropriate training;

— encourage delivery of training through small and medium enterprise associations, resource institutions, private consultants and training networks; and,

— encourage evaluation of the effectiveness of small and medium enterprise training as a part of policy review.

Another key policy measure is to encourage the active participation of the social partners in all aspects of planning, design and evaluation of training strategies. The ILO has been directly involved in the creation of more than 60 tripartite productivity centres in all parts of the world, many of which focus a substantial part of their activities on small and medium-sized enterprises. These centres involve representatives of employers, workers and government in providing services which enable enterprises to enhance their productivity and competitiveness. Services include improved management training, labour relations, consultancy support and innovative information on management of quality control, employee motivation and safety and health.

Despite such measures the vast majority of micro-enterprises do not benefit from institutionalized sources of training. Rather, learning takes place on the job and through a range of informal apprenticeship systems. Experience from a number of developing countries indicates, however, that associations of micro-enterprises can play an important role in providing or facilitating access to training, as can other structures such as common facility centres (see Chapter IV).

### *Social protection*

Employment is the most important guarantee of social protection in both the organized and the unorganized sectors. It provides the basis for earnings, part of which can be saved for insurance — private or social. Many workers in small and medium-sized enterprises, however, are excluded from basic health insurance and insurance of their homes, possessions and family and against loss of income.

Frequently, the administration of social security systems is not able to deal with the special circumstances of self-employed and casual wage workers. When formal social security is extended to smaller enterprises, each employer has to be identified and registered and then taught and persuaded to comply with the rules for registering employees and with the procedure for paying contributions. In the case of casual

workers, contributions are difficult to secure and maintaining correct records is administratively awkward when work is intermittent and undertaken for different employers.

Formal social security schemes have therefore often experienced problems that have resulted in a loss of confidence among their members. These difficulties stem from such factors as poor or patchy information on entitlements, failure to take into account the damaging effect of inflation and the consequent need to adjust contributions and benefits (particularly pensions).

Given the difficulties experienced with many protection schemes, improvements are being sought and countries are experimenting with new approaches. Particularly promising are voluntary schemes whereby individuals join together to organize their own insurance programmes, sometimes through artisan or self-employed trade associations or in special sections of trade unions.

From the point of view of enterprises, the provision of social protection does not simply represent a cost or burden on business. On the contrary, there are clear economic benefits. Research undertaken by the Self-Employed Women's Association (SEWA) in India has shown that the availability of health insurance and child care keep women workers in good health and provide them with peace of mind that permits them to concentrate on their jobs and raise their productivity.

### *Labour standards*

All workers, including the self-employed in every size of enterprise are covered by a number of ILO international labour standards (ILS). Some of these reflect such basic human rights as:

— freedom of association and collective bargaining;
— protection against forced labour and discrimination;
— elimination of child labour;
— occupational safety and health.

National legislative provisions give effect to ILO standards and reflect national policies for the protection of working people. In principle, this body of national and international labour legislation applies to all workers. The conditions of SMEs, however, create exceptional circumstances, since they may lack the capacity to meet the labour standards expected from large enterprises.

Many international and national instruments of labour law therefore contain exemptions and specific provisions designed to reflect the economic circumstances of small and medium-sized enterprises and seek a balance between, on the one hand, fostering this potentially important source of employment and, on the other, maintaining acceptable labour standards. Recently, this issue has acquired renewed importance due to the fact that, after many years of apparent decline when SMEs were viewed as relics of an outdated economy, the proportion of workers in small and medium-sized enterprises in industrial countries is increasing again (Potobsky, 1992). Many SMEs in developing countries also provide (frequently marginal) employment but fail to meet minimal legal standards because of poor management, prohibitive cost or lack of local enforcement.

Small and medium-sized enterprises are often accorded different treatment and sometimes are even totally excluded from the application of labour law. In other cases,

dismissal is made easier and less expensive for SMEs, although recent legislation in several countries suggests a trend toward wider application of employment protection laws.

The legal right to worker representation in enterprises has traditionally excluded small and medium-sized enterprises (as variously defined in different countries and sectors). For example, in Austria and Germany works councils must be established in enterprises occupying five workers or more on a permanent basis. In Spain the appointment of workers' delegates is optional in enterprises employing between six and 12 workers, but is mandatory beyond that threshold; in enterprises with 50 workers or more a workers' committee must be established. In many countries, the applicability of national occupational safety and health standards also varies widely according to the size of the enterprise. An examination of national legislation suggests, however, a distinct trend towards extending the rights of worker representation to small and medium-sized enterprises (Potobsky, 1992).

On a number of issues it is generally accepted that certain labour protection rules may not apply to SMEs. For example, in Austria the provisions relating to protection against dismissal are incorporated in the Works Constitution Act and therefore only cover the workers who fall within the scope of the Act. In the Republic of Korea the provisions of the Labour Standards Act may be extended to enterprises continuously employing fewer than four workers, and in Sri Lanka the Termination of Employment of Workmen (Special Provisions) Act, No. 45 of 1971, does not apply to enterprise employing fewer than 15 workers. In Argentina a law was recently adopted whereby workers of SMEs (i.e. workers in enterprises employing fewer than 40 workers) are entitled to shorter notice periods than those of bigger organizations. This law also allows for a certain amount of flexibility as concerns the application of general labour law, legislation, subject to agreement through collective bargaining; to this end, it makes it mandatory for sectoral-level agreements to include special provisions relating to SMEs. In Panama, under a law of 1986, unfairly dismissed workers of small enterprises are entitled to compensation but not to reinstatement, which is granted to workers of bigger enterprises; and overtime compensation in small enterprises is paid at a lower rate than in bigger organizations. In a few countries such as Bolivia and Honduras labour legislation does not apply to small rural firms, yet it would seem that there is now a tendency to place all rural firms that employ wage-earners within the scope of the Labour Code. This has been done in the 1992 Labour Code of the Dominican Republic, and is also foreseen in the revision of the Labour Code of Honduras, now under way. In other countries, especially in Africa, labour law usually does not apply to small enterprises, provided they are family businesses and do not employ wage-earners other than those that are members of the owner's family. Given the broad definition of "family" in Africa, a qualification is often added to such an exclusion so that it does not include bigger SMEs; in most cases, there is a threshold of five workers, beyond which the labour law ought to apply. None of these variations implies the actual exclusion of SMEs from the general scope of labour law.

The views of legislators, employers and workers on the applicability of general labour standards sometimes vary, reflecting the competing demands of reduced regulation, economic stimulus and safeguarding equitable standards of employment. The ILO opposes any kind of deregulation which abrogates the most essential protective legislation or opens the way to unsatisfactory or exploitative conditions. It would, however, accept both the elimination of unnecessary provisions (or their

replacement by others producing desired results with less bureaucracy) and a more flexible application of regulations, if balanced by other acceptable measures under union control.

Small and medium-sized enterprises sometimes face special difficulties in applying labour legislation which was not conceived with their specific characteristics in mind. This is why employers, workers and policy-makers tend to express concern over both differentiated and undifferentiated regulatory arrangements. The current worldwide expansion of the small and medium enterprise sector increasingly demands a regulatory framework adapted to the specific character of SMEs, which reconciles the fragility of many small and medium-sized enterprises with the need to secure reasonable rights for their employees, yet does not contribute to the erosion of standards in enterprises that are strong enough to meet them. What is required is a means of adjusting national and international labour law to the characteristics of small and medium-sized enterprises (Servais, 1994).

In formulating each country's response to the challenge of reconciling these views and interests, due regard needs to be paid to the flexible formulas provided for in many ILO instruments. Consideration should also be given to whether special legislation adapted to the needs of carefully defined SMEs would best contribute to stable law and practice while, at the same time, ensuring support for a growing small and medium enterprise sector and maximizing the quality of the employment which it generates.

Labour regulations need to be continually assessed for their short and long-term effectiveness and cost impact, not only on individual enterprises but on the broader economy. For example, failure to adhere to safety regulations might save money in the short run but could have very expensive consequences in the longer term. Moreover, as explained later in this report, failure to ensure adequate working conditions undermines productivity and profitability and sets back attempts to achieve a culture of quality and constant improvement. Reviews of the policy and regulatory framework should thus bear well in mind the special conditions and constraints which apply to the small and medium enterprise sector without compromising the basic principles of international labour standards. Good working conditions, security and fairness are an integral part of a wider small enterprise development strategy to promote efficient and competitive enterprises.

## 4. Reducing regulatory constraints on the development of small and medium-sized enterprises

A burdensome or inadequate legal and regulatory framework can be an obstacle to small enterprise development. The lengthy bureaucratic processes to comply with multiple legal requirements and import/export rules or to benefit from government incentives are often beyond the means of small firms. Regulations can be too numerous or not well implemented or not easily understood.

Legislative obligations entail administrative costs which are higher per employee in small enterprises. A review of entrepreneurs in the EU found that the main problems were the complexity, number and frequency of the forms that have to be filled in and the constant changes being introduced.

The financial cost of compliance with legislative obligations for enterprises can be significant, with one estimate for the EU being between 3 and 4 per cent of GDP

(ENSR, 1995). Amongst entrepreneurs in West Africa, the primary concern was less the content of regulations than the manner of their administration. They expressed frustration at the lack of information, the overlapping responsibilities of officials and departments, the undue delays in processing applications and the tolerance by superiors of abuses of power by lower-level staff (ILO, 1994).

In countries in transition to a market economy, legal uncertainties and inconsistencies are a serious obstacle to small and medium enterprise development. The regulatory role of the State in relation to cooperative enterprises has also proved onerous in certain countries.

Administrative requirements such as registration and licencing can be a particular burden for the small-scale sector. For example, excessive bureaucratic requirements were detected in Peru, where De Soto (1989) found that it took 289 days to complete all the formalities necessary to start an enterprise. Another example was Brazil, where until the late 1970s small firms had to meet the same requirements as larger ones, with some 500 documents, signatures and permits required to establish, maintain and liquidate a firm. In Uzbekistan business registration is a highly complex procedure. Potential entrepreneurs have to visit a number of agencies with a range of different information and supporting documentation (White and Petterson, 1995). In one East African country, small traders are required to have separate licences for selling different categories of products such as groceries and vegetables from the same stall (ILO, 1994).

A recent study of small entrepreneurs in Bangladesh, Nepal and the Philippines found that requirements and procedures for registration and licencing entailed considerable transaction costs. In Bangladesh and Nepal in particular, the majority of respondents reported delays, hidden costs and bureaucratic procedures when dealing with public administration. Steps are being taken to simplify procedures. Now, any Nepalese enterprise has the right to be registered within 21 days, compared to three or more months previously. The Philippine Government has gone one step further by introducing special legislation for small firms. Under the Kalakalan 20 Act small rural industries have only to submit a one-page application to the municipality to become registered (Meier and Pilgrim, 1994).

Elaborate regulations restricting the establishment and operation of small enterprises are extremely difficult to enforce, and attempts to apply them fully are often self-defeating. Studies undertaken in Benin and Tunisia concluded that such attempts would seriously impair incomes and employment in micro-enterprises and would produce a socio-political backlash from the urban poor. The Tunisian study recommended reducing regulatory requirements to a minimum and then vigorously enforcing them (ILO, 1994).

## 5. Strategies for continuous review of small and medium enterprise development policies

### *National strategies*

Small firms are moving out of the shadow of large companies. They are increasingly being viewed as a form of organization that requires specific policies and institutions tailored to its needs. Small and medium-sized enterprises are not

scaled-down versions of large firms. Many public and private agencies are therefore now examining with small firms the appropriateness of policies geared essentially to large firms and organizations and are looking very closely at the special needs of small enterprises.

Small firms often have problems with finance, productivity, information management, skills, marketing and, increasingly, internationalization, as well as with an inadequate regulatory environment. Policy approaches towards small firms must take account of the kind of organization involved and allow for such factors as lack of scale, resource limitations, local character, and the need to coordinate actions.

In recognition of these particular characteristics and needs, many countries have comprehensive plans or programmes aimed at the small and medium enterprise sector. For example, the Republic of Korea, recognizing the need for more adaptability and diversification in a production system hitherto dominated by *chaebols*, in 1988 launched a long-term plan for the small and medium enterprise sector. In Singapore the Government brought out a Small and Medium Enterprise Master Plan in 1989 which calls for an integrated multi-sectoral approach to the promotion of SMEs (Regnier, 1994). Japan also has a very comprehensive SME policy which includes provision of special financing arrangements, preferential tax treatment, establishment of support institutions, improvement of technology, informatization, management and labour conditions, assistance with exporting, and promotion of cooperation, networking and subcontracting.

In 1995 South Africa launched a national strategy for the development and promotion of small business, involving a wide-ranging policy and support programme focusing on nationwide access to services such as finance, marketing, opportunities, training and export support, rather than on the provision of subsidized loans to a few small and medium-sized enterprises. Namibia and Malawi also have national programmes for small enterprise and informal sector development. Kenya has a strategy for small-scale and Jua Kali enterprise development, and the United Republic of Tanzania has adopted a special national policy for informal sector development.

In Colombia the Government formulated a national plan for the development of the micro-enterprise in 1984 which has been refined over the years. The plan supports small enterprises by improving credit facilities, technological services, entrepreneurial training, marketing services and the institutional framework.

Small and medium enterprise plans or programmes can be coordinated by a specially dedicated government ministry, as in Belgium and Luxembourg, or by a department within a ministry, such as the Ministry of Industry. In France the mandate of the Ministry of Enterprises and Economic Development includes small and medium enterprise policy. In the Netherlands one of four departments of the Ministry of Economic Affairs deals with entrepreneurship and small and medium-sized enterprises (ENSR, 1994).

Elsewhere, small and medium enterprise programmes are frequently run by semi-independent apex institutions that are formally answerable to one or more ministries but in practice operate with considerable autonomy. The creation of such institutions is a growing trend in many parts of the world and is considered in Chapter IV.

### *Committees for review of policies and regulations*

Economies have become so dynamic that it now behoves governments to continually monitor policies continually to ensure that they fulfil the functions and objectives for which they were initially formulated and that they do not contain unforeseen biases against specific sectors such as small and medium-sized enterprises. Many countries are now establishing high-level advisory committees, often including representatives of the private sector, to evaluate existing policies and regulations and, if necessary, recommend improvements (see box 3.5). Sweden, for example, created a Deregulation Commission in 1993 which undertakes a rolling review of rules affecting companies. Reforms have been carried out in areas such as the registration of new enterprises and tax deductions for entrepreneurs.

**Box 3.5. United Kingdom: Deregulation Initiative**

The Government of the United Kingdom has placed a great deal of attention on the need to reduce administrative burdens on all enterprises, and in particular on small and medium-sized enterprises. The major outcome of this is the Deregulation Initiative, a twin strategy of reviewing existing regulations, and rigorously evaluating new regulations. In its review of the existing regulatory system (in close consultation with business), the Government has identified over 500 measures requiring action, including health and safety legislation and environmental legislation, and a rolling review of regulations will be established in the future. To avoid possible burdens caused by new legislation, all new regulations likely to impose a burden on enterprises are subject to a compliance cost assessment and, where appropriate, an assessment of risk.

Another important strategy in the United Kingdom is the simplification of administrative procedures, and special attention has been paid to small and medium-sized enterprises in respect of reporting requirements.

Source: ENSR: *The European observatory for SMEs*, Third annual report (Zoetermeer, Netherlands, 1995).

In Portugal the Government has adopted the recommendations of a Business Administration Commission as part of an interministerial programme for debureaucratization. The programme contains about 90 proposals for administrative simplification in such areas as the registration of new enterprises, fiscal and statistical requirements and obligations related to international trade. The latest proposals of the commission give special attention to the simplification of administrative procedures and improvements in the transparency of legislation, information and the interaction between the public and private sectors (ENSR, 1995).

Norway has established a Business Legislation Committee to examine legislation that affects the possibilities of business development, particularly for small and medium-sized enterprises, and to propose simplifications and other changes to stimulate business activity.

In Mauritius an advisory board regularly reviews measures, including incentives, to promote small and medium enterprise development.

In China business regulations are reviewed and improved regularly, taking into account the interests of small and medium-sized enterprises (UNCTAD, 1995a).

A recent review of strategies, policies and measures to reduce administrative burdens for SMEs has been undertaken in the European Union. It was found that all countries were using at least three of the following approaches:

- information and advice concerning requirements and administrative procedures;
- simplification of administrative forms;
- creation of special rules for small and medium-sized enterprises;
- replacement of existing laws;
- evaluation of possible effects of new legislation;
- research into administrative burdens on small and medium-sized enterprises.

### *A consultative and decentralized approach*

The formulation of new policies for small firms is increasingly accompanied by governments' readiness to consult, involve and assist the social partners, especially in areas related to the regulatory environment. At the same time, there is a strong tendency for policy implementation, and sometimes policy formulation, to be decentralized down to the local level. Some regulatory burdens are eased by dealing with registration and licencing applications, taxes and other requirements at the local level, thereby facilitating communications, speeding up processing and reducing time lost travelling. There is also some indication that some policies and regulations might in future be geared more to the specific conditions prevailing in particular areas.

In the United Republic of Tanzania the ILO has been providing advice on the formulation of a new national employment policy which will provide a national institutional framework for micro-enterprise promotion. A National Directorate and district level centres will be established for micro-enterprise promotion. The creation of such institutions will be accompanied by an array of policies to create an enabling environment for SMEs by, for example, minimizing regulatory impediments, improving training and access to finance, providing support services and promoting basic labour standards. The private sector will be brought closer into the policy formulation process, partly by strengthening informal sector associations.

Through its COOPREFORM programme, the ILO also assists governments and cooperative movements in the review of their cooperative legislation and development policies to bring them in line with the requirements of the market economy.

### *Statistical data as an important input to policy-making*

Policy formulation, implementation and monitoring in the area of SME development is severely hampered if there is a shortage of data on the SME sector. Few countries have readily available data on small and medium-sized enterprises under their present system of labour statistics. SMEs therefore need to be covered either through the regular statistical sources or through special studies. The most important potential regular source of data on small and medium-sized enterprises is

establishment surveys (surveys of employers) and administrative records (business registers, social insurance schemes, etc.). In these, information is generally provided by employers, who are in the best position to supply data on the characteristics of establishments, such as the number of persons employed, wages paid, hours worked, information concerning production (inputs, costs, outputs, etc.) and financial matters.

In reality, establishment surveys and administrative records are subject to constraints in a number of countries. This makes it difficult, and sometimes even impossible, to use them for compiling data on small and medium-sized enterprises. Household surveys for measuring the labour force, the third major source of regular labour statistics, are not well suited to the collection of information about establishments, as the respondent is the individual worker, who normally would not have access to the required information. In some countries, special studies are carried out, but these tend to fall outside the regular labour statistics system.

The paucity of official statistical data on SMEs became apparent during the preparation of this report. The gaps in coverage are particularly wide in the developing countries and the transitional economies. This makes it difficult to draw reliable conclusions about the characteristics of small and medium-sized enterprises, how they differ between industries, countries and firm size, or how they have changed over time. Data related to working conditions in SMEs are especially scarce. A greater emphasis on statistical reporting and analysis would lead to a better understanding of the strengths and weaknesses of small and medium-sized enterprises, would allow their impact on SME development policies and programmes to be better monitored and evaluated, and would enhance accountability for the public resources devoted to the sector.

A step towards the development of official statistics on SMEs was made by the Fifteenth International Conference of Labour Statisticians (Geneva, 1993) through the adoption of its resolution concerning statistics of employment in the informal sector, which in many countries account for a significant proportion of SMEs. The resolution provides technical guidelines to member States regarding, inter alia, the definition and classification of informal sector enterprises, the measurement objectives and types of data to be collected, and data collection methods and programmes integrated into the regular national statistics systems.

The ILO has also recently developed a methodological framework for surveying the informal sector. This methodology, which has been documented in a manual, is being used in a number of countries (Benin, Philippines, United Republic of Tanzania and some countries in Latin America).

# CHAPTER IV

# BUILDING SME CAPACITY TO CREATE JOBS

## 1. Introduction: The varied requirements of SMEs

Because of their small scale, lack of resources and tendency towards specialization, SMEs are highly sensitive to the calibre of the public and private services at their disposal. Unlike large fully integrated enterprises, smaller units often do not enjoy all the upstream and downstream advantages for developing and marketing their products and services. Therefore, there is a need, within an enabling environment, for services, institutions and programmes to facilitate the growth of small firms, expand employment and help meet social needs.

In some countries effective support programmes already exist. In others, however, programmes and services are often ill-adapted to the needs of small firms, especially in the context of present global change. In many developing countries and countries in transition public intervention will be required, since market forces alone are unlikely to create an adequate service infrastructure.

However, SMEs typically rely on a wide variety of informal sources of information, skills development and other expertise rather than on more institutionalized services. Equipment suppliers and manufacturers are the main sources of technological support, while wholesalers, retailers and exporters, competitors and other SMEs tend to be important sources of marketing information. Private consultants often provide important services to SMEs, and magazines published by sectoral associations are another valuable source of information. The institutionalized service infrastructure must clearly recognize and capitalize on these informal information and support structures. This chapter will therefore also deal with strategies to facilitate inter-enterprise linkages and similar mechanisms, as well as the critical role of SME associations.

### *General problems of small and medium-sized enterprises*

Small and medium-sized enterprises experience many difficulties related to their scale of operations and resource limitations, and often also because of their newness. Some problems have been prevalent for many years, while others are coming to the fore as global economic trading conditions change. They include:

- low levels of productivity associated with inadequate technology, poor skills and inefficient organization;
- weak management ability, especially in firms wanting to grow;
- poor access to credit for both working capital and longer-term investment, especially from formal sources;

— lack of access to information about markets, suppliers, operational techniques, new designs, regulations and standards;
— difficulties in innovating (increasingly important in a fast-changing competitive environment);
— weak ability to internationalize, a particular problem for small firms and one which has become of paramount importance as economies become increasingly integrated under pressures of globalization;
— difficulties in meeting rising world expectations regarding quality standards;
— inadequate working conditions and levels of social protection, which are not only detrimental to workers but also to the capacity of the enterprise to innovate and improve productivity.

Of course, not all small firms exhibit these characteristics. Many are innovative, productive and efficient, and provide good pay and working conditions.

This section describes the kinds of services provided, the support institutions and their principles of operation, and the programmes dedicated to helping small firms become sustainable and productive.

### *Differences in needs*

Small and medium-sized enterprises and entrepreneurs have different needs. Size, and degree of development, are important differentiators. New enterprises require different support from established enterprises, and those wishing to start new businesses are likely to require different approaches. These will depend on such factors as: differences in gender, age, ethnic and religious traditions; the unemployment context; the process of large-firm disintegration and spin-offs; franchising possibilities; and special circumstances such as the demobilization of military personnel.

Once established, growing small firms require different services at different stages of growth, such as when a certain size or level of technological complexity is reached.

Furthermore, firms are likely to have sector-specific requirements, differentiating the particular organizational, technological and market peculiarities of, say, garment production and food processing. Equally, firms in the services and extractive sectors have priorities and needs different from manufacturing firms. Moreover, the needs differ even within sectors, according to the markets served and the basis on which the firms compete. Distance between firms and service sources, and between competing firms, also have implications for policy and service delivery. Finally, of great importance is the legal and regulatory environment, presenting entrepreneurs with many challenges of compliance with taxation requirements, size and weights standards, and import/export rules and procedures.

## 2. Principal types of support services

### *Overview of support services for small and medium-sized enterprises*

Services required by SMEs include:

— *finance* provided by institutions serving a broad client base or focusing specifically on small firms;
— *training* provided by public and private institutions, individual firms for their own staff, private sector associations and chambers of commerce;
— *information* on markets, technology and regulations provided by public business information centres, private consultancies and private "self-help" associations;
— *quality testing and measurement services* and a range of advisory services on, for example, taxation and law provided by public and private agencies.

The most common services, several of which are often delivered by a single institution or programme, are discussed below.

### *Finance and credit*

Shortage of credit is possibly the most serious problem for small firms. The reasons, which have been outlined elsewhere in this report, include high transaction costs, high risks, lack of collateral, complicated loan application procedures, and in some cases generally inadequate financial service infrastructures.

### *Training*

Training programmes can serve to:
— impart information on changes in the regulatory and broader environment;
— provide basic financial skills (managing cash flow, debtor/creditor relations, costing, etc.);
— enhance entrepreneurs' negotiating, selling, persuading and other "soft" skills;
— in terms of business development, offer insights to problems and opportunities arising from survival and growth (Gibb, 1995).

Training should be provided close to the enterprises since small entrepreneurs cannot afford to be away from the enterprise for long periods. The type of training provided should be based on an assessment of the specific needs of the enterprise. For example, multidisciplinary skills are essential and need to be acquired on the job. Sometimes, training is taken to the enterprise by mobile workshops. Growing in importance is the "mentor" approach, whereby entrepreneurs and workers learn from their peers by visiting one another's workshops and discussing the best practice in experience exchange groups. The pace of change is now such that the need for training and retraining will acquire increasing prominence in future years.

The ILO has developed a number of standard packages such as "Improve Your Business" and "Start Your Business". These are easily adaptable to local conditions and are used in more than 60 countries worldwide (see box 4.1).

**Box 4.1. ILO's global Improve Your Business Programme for SMEs**

The Improve Your Business (IYB) Programme is a system of interrelated training packages and support materials to provide SME owners and managers with basic business management skills. The Improve Your Business Programme provides institutions and individuals who are involved in management training for SMEs with a comprehensive set of materials for a variety of target groups. It deals with various topics related to small enterprise development such as training, business extension and follow-up training, and monitoring and evaluation.

The following packages are available: Improve Your Business, aimed at SME managers wanting to expand their business; Improve Your Business Basics, aimed at entrepreneurs with only basic education; and Start Your Business for business starters. In addition, a monitoring and evaluation system has been developed to assess programme impact continuously. Business extension services provide methods for follow-up training and consultancy, while trainer guides provide guidelines on how to plan and conduct training. The IYB business games provide a practical and lively simulation of managing a business.

The IYB Programme is used in more than 60 countries and has been translated into over 30 languages. More than 100,000 entrepreneurs have benefited from the materials to date. Several evaluations indicate that the majority of entrepreneurs who participate in courses are able to translate lessons learned into improved business performance.

*Information*

Acquisition of information is crucial for small firms, ranging from basic matters like laws, regulations and standards — particularly important in transition economies where the regulatory framework is changing — to alternative sources of supply and alternative prices, market trends and fashions, and the latest techniques and technologies. The means of communicating information are also critical. Institutions serving small enterprises can employ economies of scale, form links with a range of information sources, and coax competing firms to pass on ideas.

Efficient garnering and use of knowledge has become a basic source of competitive advantage. Therefore, policy-makers have increasingly sought ways to improve small firms' access to knowledge, and hence their capacity to innovate. Thus, universities and other institutions are encouraged to share knowledge through special transfer centres or science parks. Multinational companies are encouraged to import knowledge of best global practice, and service institutions are encouraged to join international information networks.

*Marketing*

Advice on marketing is important, including packaging, product design, participation in fairs, production of advertising brochures, fashion information, regulations and specifications in different countries and research on markets, competitors and suppliers. Assistance with client contacts via computerized

databases, or through programmes of institutional and interregional cooperation, is growing. Many small firms cooperate to market and export their products and services, and trade associations facilitate international access. Subcontracting to large firms and encouraging firms in export zones to use local small-firm suppliers are also increasingly common.

### *Technology*

Low productivity, poor quality, limited product capability and outmoded technology are common problems in small enterprises, and the scope for technological support is therefore great. It needs to be differentiated by sector, and by size and sophistication of the enterprise. The services required by capital-intensive small firms are different from those required by informal-sector workshops. Clothing production needs different help from electronics, chemicals, catering or footwear.

Technology services must be sensitive to the particular needs of clients, which might demand simple, cheap solutions, or state-of-the-art technology. Most successes have been achieved when industry service centres have adapted existing technology to specific needs. Many technologies are applicable sector-wide or industry-wide. Engineering machinery and some computerized information systems are examples. Service institutions disseminate generic technologies by providing training courses, often employing demonstration technology, encouraging leading local firms to act as demonstration cases, or providing common facilities centres which small firms can use on a fee-paying basis. This is the case with sophisticated quality testing and measurement machinery, for example.

Some service agencies offer customized services to solve specific technological problems, and in some countries such as Germany individual technology consultancy services to small firms are common. However, this can be costly for the small enterprise, and many institutions choose to provide more general services. Technology services are often provided along with advice on finance, training, working conditions and the organization of work. Improvements in one direction may be constrained by inadequacies in another, leading to demand for further advice and support.

An important source of ideas on technology, and finance to introduce it, can be suppliers of materials and equipment, and large-firm customers, often the local plants of multinational organizations. There are many cases of large firms helping to upgrade their suppliers, and in recent years programmes encouraging this have become common. Thus, service institutions can help to transfer technology by facilitating large-to-small firm linkages and, through integrated advisory approaches organized on a sectoral basis, to reach and improve the operation of deficient suppliers.

## 3. Institutional strategies

Recent years have seen a much greater involvement of the private sector in delivering services to small and medium-sized enterprises. The aim is to make support services relevant to client needs and to develop a leadership role. For example, institutions promoting technology transfer should both respond to what their clients require and offer the best solution from the forward-technology standpoint.

The predominant trend now is to become more client-responsive by:

— decentralizing delivery so as to be as close to the clients as possible;
— introducing a greater degree of market influence in determining which services are suitable;
— involving trade associations and sometimes trade unions in the governance of the service institutions.

This responsiveness is often further strengthened by making service institutions sectorally and size focused. The movement towards providing decentralized services that are tailored to client requirements has been accompanied by a recognition of the need to ensure a coherent and coordinated approach. Many small firms require packages of interrelated services which can be most effectively supplied through a network approach whereby service providers offering different services are encouraged to cooperate with one another in ensuring individual client needs are met. Networking further serves to identify weak points in the service system which can then be corrected. The movement towards an integrated approach also increasingly involves integrating services provided by a decentralized support network with other programmes and policies, of both a regulatory and promotional kind. Special agencies at national level, and sometimes also at regional and local levels, may be created to carry out the coordinating and integrating functions.

Three broad types of institution offer services to small and medium-sized enterprises: institutions to facilitate credit access; small business development centres; and facilities and supporting services of business incubators, common facilities centres, industrial estates and science parks.

### *Institutions to facilitate access to credit and other financial services for small and medium-sized enterprises*

Small and medium-sized enterprises are heterogeneous; their financial needs vary by size, activity and location. Micro-enterprises often need short-term credit in small amounts, while the more dynamic small enterprises may require longer-term finance to upgrade facilities or to overcome shortages of working capital. Small firms have particular difficulty gaining access to finance from formal institutions, because of banks' avoidance of risk, high transaction costs, lack of suitable collateral, and complicated procedures. As a result, informal financing arrangements have evolved, especially in developing and transition countries. (Some examples of national credit programmes are given in box 4.2.)

From among the formal financial intermediaries the following types need to be singled out, either because of the magnitude of their dealings with small enterprises or because of their potential to become important financing partners of SMEs.

Commercial banks offer perhaps the widest range of financial services. Also, they dispose of a dense branch network and are generally professionally managed. This potential is, however, usually not available to small enterprises primarily because of the high risk associated with small enterprises. In some developed countries such as Japan this may not always be the case. Particularly during periods of economic downturn with stagnating demand for finance from larger enterprises, commercial banks are willing to lend to SMEs which are unable to meet formal collateral

**Box 4.2. Examples of national credit programmes for small enterprises**

Countries are liable to have a variety of institutions supplying finance to small enterprises. In *Japan* there are several agencies which provide loan guarantees, including the Small Business Credit Insurance Corporation. Also, the Government has established four special banks for long-term, low-interest loans to small firms: the Small Business Finance Corporation, for long-term credit required for modernization and rationalization; the People's Finance Corporation for smaller firms; the Central Cooperative Bank for Commerce and Industry, for cooperatives; and the Environmental Sanitation Business Financing Corporation. The Government has further created a special SME Investment Corporation which invests in small-scale entrepreneurs, especially those engaging in high-risk ventures where the profits are too low to attract commercial banks. Primary targets for investment include new venture business, local but labour-intensive business, and business important to other industries.

In the *Republic of Korea* two special financial institutions have been established for SMEs: the Small and Medium Industries Bank, and the Citizens National Bank, both established with government assistance and providing both short-term and long-term finance for small firms.

In *Poland* four financial intermediaries provide the majority of credit to SMEs:

- the Cooperatives Umbrella (BGZ) which oversees the activities of Poland's cooperative banks (which act like credit unions);
- the Polish Development Bank which provides medium- and long-term financing and venture capital for medium, small and micro-enterprises in Poland;
- the Bank for Social and Economic Initiatives which is a government-controlled institution that supports the growth of small firms;
- the Polish American Enterprise Fund, financed by the SEED Act of the United States Congress.

Source: APO: *Promoting information technology in small and medium industries* (Tokyo, Asian Productivity Organization, 1994); and GEMINI: *Small enterprise development in Poland: Does gender matter?*, technical report No. 73 (Bethesda, Maryland, 1994).

requirements, provided adequate trust exists and financial and managerial information is disclosed.

Development banks intervene in areas with low immediate financial returns but considerable expected social and economic benefits. Small enterprise finance is one such area. Virtually all such institutions have special "windows" to provide long-term finance to small and medium-sized enterprises. In Asia the Industrial and Financial Corporation of Thailand and the Development Finance Corporation of Sri Lanka have developed separate SME lending units. In Africa the Development Bank of Zambia, together with other Zambian institutions, has established a development service for SMEs, while the Botswana Development Finance Corporation and National Development Bank have set up Tswelolo Limited to provide them with loans.

The drawbacks of development finance institutions (DFIs) from the standpoint of small-enterprise finance are the absence of a branch network, the limitations on the kind of financial services they can offer and the limited resources available for the many small enterprises. It is therefore generally acknowledged that DFIs can only have a pilot or demonstration function in small-enterprise finance.

To involve commercial banks more in small-enterprise finance, many governments have set up guarantee funds to share the risk of loan default. The Small Business Guarantee and Finance Corporation (SBGFC) in the Philippines provides guarantees to encourage financial institutions to approve loans on this basis. Sometimes, the guarantee capital is put up directly by aid agencies and entrusted to NGOs. This is the case of an interregional project that the ILO is implementing with the RAFAD Foundation and six different NGOs and self-help organizations. The project seeks to strengthen NGO capacity to manage the guarantee fund professionally and to negotiate better leverage with commercial banks (Bastiaenen, 1995).

Other small enterprises, particularly the more dynamic and fast expanding firms, are confronted with a different problem: they may have found entry into a commercial bank portfolio, but risk becoming excessively indebted because of insufficient equity capital. Here venture (or risk) capital is required to overcome this particular financing constraint. In a recently launched project in Zimbabwe, the ILO is bringing together different small-enterprise promotion and financing agencies to address this issue (Bastiaenen, 1995). Banks, large corporate investors, pension funds, insurance companies and private venture capital companies are typical sources of venture capital. In Asia countries such as India, Indonesia and the Republic of Korea have set up venture capital funds; the Republic of Korea has 58 venture capital companies, which tend to invest in technology-intensive manufacturing companies with high growth prospects and high expected profits (Park, 1993). In Mexico a government industrial development trust fund, FOMIN, administered by the National Development Bank, provides minority contributions to SME equity capital. International venture capital funds, created by donor institutions for investment in developing countries, include the Commonwealth Development Corporation and the French Société d'Investissement et de Développement International (SIDI).

The main problem for equity finance corporations set up specifically for small enterprises is the difficulty of composing a financially viable venture capital portfolio exclusively with small enterprise participation. Also, the long gestation period before profits are generated and the need to devise set modalities for participation pose more problems for small-enterprise venture capital institutions than for those focusing on larger firms.

Savings banks can be an important source of finance for small and micro-firms and have in many countries been their most important financial partner. Municipal authorities have often selected savings banks to offer an opportunity for small savers to make deposits and at the same time keep the collected resources in the local economy. In many European countries this social commitment to local economic development is reflected in certain tax advantages and in a guarantee provided by the municipal authorities.

A similar social mandate characterizes cooperative banks for agriculture and manufacturing. Examples of the latter are France's Banques Populaires and Germany's Volksbanken, which cater specifically to small enterprises and crafts. These cooperative banks have a network of agencies in rural and urban areas.

Credit cooperatives are a major source of capital for their members in many countries. In 1993 the number of institutions affiliated to the World Council of Credit Unions in Africa, Asia, the Caribbean and Latin America totalled more than 37,000, with almost 15 million members and over US$14 billion in assets.

In Indonesia many people, especially self-employed small traders, join together to organize savings and credit cooperatives. In the Philippines the Baclaran Vendors (Credit) Cooperative has around 2,000 members. By all accounts it has been very successful and provides its members with a range of other services, including training, dental services and business linkages (Hansen, 1995).

Industrial and commercial credit. Other forms of non-bank credit are supplier and customer credit and credit arrangements for subcontracting purposes. For example, larger enterprises might "lend" raw materials on the understanding that the materials will be used for making products to be bought by the lender; the cost of the raw materials will then be deducted from the payment for the finished products. The need for working capital is exacerbated when payment for goods is slow. In some countries, such as Japan, there is special legislation protecting SMEs against slow payment by big customers. Letters of credit issued in connection with the export orders can also be an important source of SME credit when appropriate discount facilities are available.

Informal credit arrangements. Small borrowers, or new borrowers proposing risky ventures or possessing few assets to offer as collateral or for whom speed of delivery is essential, have recourse to a wide array of informal sources, including friends, relatives, money-lenders and groups of individuals organized as mutual help associations (for example, rotating savings and credit associations).

### *Group lending schemes*

A particular financial technique that needs to be mentioned here is group lending, as it addresses the problem of the lack of collateral acceptable to a bank. This technique resorts to the traditional sanction of peer pressure to ensure the payment of a debt — a modern loan contract. Many successful small-enterprise financing schemes have adopted some form of group liability. Perhaps the best known example is the Grameen Bank of Bangladesh. By the early 1990s Grameen had over 800,000 borrowers and disbursed over $100 million a year. Grameen lends money on an unsecured basis using five-person group guarantees, meaning that each individual is responsible for the others and future access to credit is determined by all members paying their loans. The size of Grameen loans ranges from $10 to $160, with an average size of $60. The Grameen Bank has maintained a 97 per cent recovery rate. A subregional ILO survey of collateral substitutes found that instruments such as group liability, blocked savings and interlinked contracts can indeed protect a bank against losses just as well as conditional guarantee instruments (Balkenhol and Llanto, 1995).

### *General strategies for small-enterprise finance*

Experience shows that for finance schemes aimed at smaller businesses to operate on a viable, sustainable basis they have to: cover their costs, separate financing and non-financing functions, apply sanctions against defaulters, take into account the

price of capital on the local market, and offer savings facilities. This type of scheme is most likely to be successful in a liberalized, competitive financial sector with a strong but flexible supervisory authority.

### *Small business development centres*

Business development centres have grown rapidly in recent years. They include entrepreneurship support centres, local economic development agencies, local service centres, and "real" service centres. Generally, these are decentralized institutions which provide small enterprises with a range of support services, varying in scope according to need and circumstance.

The most common service provided is information on subjects ranging from general regulatory procedures to markets, suppliers, fashions and technology. Also common are training courses on bookkeeping and accounting procedures, pricing, marketing, quality control, management, skills upgrading, etc. Some of the bigger centres offer assistance in such areas as research consultancy, quality testing and measurement, design, packaging, finance, organizing business networks, productivity improvement, working conditions and new organizational practices.

Development centres offer either a comprehensive package of services or specific services, which often involves referral into a network of specialized centres. This comprehensive approach, together with the local character of the services provided, helps to minimize the time required from the entrepreneurs. Efforts are made to make centres client responsive, often by charging for services, by including private sector representation on their executive boards and, increasingly, by linking centres to groups like sector-specific credit or trade associations. Sometimes, a proactive development approach is required, for instance to carry out local development strategies or promote particular sectors. Focusing services on a particular sector or size of enterprise improves the centre's expertise and effectiveness. Charging for services also helps achieve sustainability, although developmental services often require some external subsidy, especially in disadvantaged sectors. The coverage of service centres and the extent of services provided vary according to the other services available, such as those of trade associations and private consultancies.

Successful programmes operate in many countries. In the Emilia Romagna region of Italy, "real" service centres either are sector-specific and locally based near the industry, or are cross-functional, providing general services to a range of industries. The centres form a network coordinated by a central agency, which complements their services with those of other agencies, including entrepreneurial associations. In Spain the region of Valencia has a well developed network of technological institutes which are sector-specific, local institutions providing services according to the needs of their small-firm clients, who are represented on their executive boards through trade associations (Pyke, 1994).

Decentralized support institutions have developed rapidly in transition countries, and international donors have assisted their development. For example, the European Union's assistance programme for economic restructuring in the countries of Central and Eastern Europe (PHARE) has been active in promoting local institutions built on independent partnerships between the public and private sectors, drawing on the resources of both. In Poland alone the PHARE programme has resulted in the establishment of 32 business support and information centres (Gurbiel, 1995). These

agencies form part of a large infrastructure of institutional support for SMEs that has developed in the country and which also includes 119 self-governing chambers of commerce organized at the voivodship level to carry out advocacy functions before state authorities and provide such services as training courses, fiscal, legal and financial advice, assistance in establishing business contacts, and the organization of fairs and exhibitions.

Belarus has started establishing local entrepreneur support centres. By 1995, 14 had been approved. To gain official authorization a centre's sponsoring organization, such as a local government, trade union or employers' organization, must be represented on its board. Services include loans and loan guarantees, information, training, technical equipment and consultancy (Merkulov, 1995). South Africa has initiated a countrywide network of local service centres for small firms. Core activities include advice, information, counselling, networking and experience exchange. The local service centre network is a key element of the industrial and socio-political restructuring of the country.

In Cambodia the ILO has assisted in the implementation of an employment-generation programme following many years of armed conflict. Five local enterprise development agencies have been established to provide services which include training on how to establish or expand a business, counselling, basic training in technical skills, and small-scale loans to entrepreneurs. The agencies work closely with local government and private sector representatives, for whom they serve as intermediaries. About 2,000 small-scale entrepreneurs have been assisted, several thousand jobs have been created, loan repayment has been high, and the agencies are achieving a substantial degree of sustainability.

The ILO has also been involved in the creation of more than 60 productivity centres in all parts of the world. These centres are based on the tripartite collaboration of employers, workers and governments, and help enterprises to boost productivity and competitiveness. Practical support is given through management training, advice on labour relations, consultancy services, and information on management innovation, quality control, employee motivation, and safety and health (Henriques, 1995b).

### *Providing facilities and services: Business incubators, common facilities centres, industrial estates and science parks*

#### *Incubators*

Business incubators (see box 4.3) are aimed, for the most part, at helping new businesses. Typically an incubator consists of purpose-built or specially adapted accommodation, with equipment for offices and workshops, housing 50 or more enterprises for three or four years, until they get established. Common services are provided and paid for on a shared basis. These might include secretarial and word-processing assistance, telephone and fax, information, and expert advice on business matters. Also, the incubator can have strong links with resource agencies like financial institutions, universities, and research and development groups.

It was estimated in 1992 that approximately 2,000 incubators are operational around the world. In Canada and the United States in 1991 there were about 500

**Box 4.3. France and Spain: Two European business incubators**

The AXONE business incubator at St. Clément-les-Places in France has been set up to help scientific researchers and engineers who do not have the means to develop the technological innovations on which they intend to base their future companies. AXONE accompanies the selected projects from their inception to the start of business; it assists in the search for capital and the setting up of the business once it leaves the incubator, during which time it provides ultramodern telecommunications facilities and office equipment.

The incubator provides rent-free premises for a 12-month period (workshop and office), including overheads (heating, electricity, water and maintenance), and covers the costs of services such as secretarial assistance and advice on management, marketing and finance. From the 13th month onwards a financial contribution is expected from the business, which increases up to full market cost by the 24th month.

In Barcelona in Spain a business incubator, ACTIVA, has been established in a factory previously occupied by the Olivetti company. The municipality, the Chamber of Commerce, the Savings Bank, the economics faculty of the University, the Polytechnic and the telephone company are all members of the board of directors. An Advisory Council brings together representatives of banks, other universities, associations of young entrepreneurs and managers of small and medium-sized enterprises and cooperatives. The incubator houses 70 businesses from a variety of sectors which benefit from all the usual common services as well as specialized services of a legal, technical, financial and commercial nature and, in some cases, access to financial aid or soft loans. Established on the basis of public subsidies, the centre aims gradually to become self-financing.

Source: OECD and the Commission of the European Communities: *Innovation and Employment*, Newsletter No. 9, April 1992.

incubators, and the number was expected to double within ten years. According to a 1989 study only 14 per cent of incubator start-up companies in the United States failed within the first five years, compared with an average of 80 per cent of all new businesses (OECD and the Commission of the European Communities, 1992).

In Europe the EU has been active in promoting over 70 business innovation centres. In addition, France has over 130 project and business incubators, and Belgium has 34 enterprise centres. In Ireland and the Netherlands business incubators are frequently established in, or linked to, higher education institutions.

Incubators are also being established in Central and Eastern Europe. For example, by 1994 the EU's PHARE programme had assisted in the establishment of 14 business innovation centres in Central and Eastern Europe; by 1995 Poland alone had over 20 incubators (Mirel and Thompson, 1994; Hübner, 1995).

### *Common facilities centres*

Generally, these centres (see box 4.4) are established for small firms in the same industrial sector who share the use of commonly owned or controlled facilities,

including specialized equipment used only occasionally, design facilities, storage of materials and supplies, and training facilities. Frequently, centres provide other services in common with business development centres and other service providers.

**Box 4.4. Benin: Support through common facilities centres**

Sixty mutual savings and loan associations for different sectors such as food processing or metalworking or construction, involving 160 enterprises, have now moved on to providing themselves with expensive capital equipment on a shared basis through common facilities workshops. Three workshops have so far been established, providing: machinery and tools for use on a fee-paying basis; a unit for designing new products; storage space for raw materials and supplies that mutual associations purchase; an area to display products; and a room for meetings and training courses.

At the moment the workshops are run jointly by an ILO technical support team and a management council appointed by a board of directors elected by mutual association members. Eventually the ILO team will withdraw, leaving the institution completely self-governed by the production units it supports.

Source: C. Maldonado: *Building networks: An experiment in support to small urban producers in Benin* (Geneva, ILO, 1994).

*Industrial estates and science parks*

Industrial estates offer entrepreneurs sites with basic infrastructure such as roads, water, power and telecommunications, and premises for rent or sale — often under very favourable conditions. Common service centres and consultancy services can also be provided. Many such estates are to be found in industrialized countries.

Both India and Pakistan have many government-sponsored estates, offering facilities in and around major towns and cities. In Turkey industrial estates often arise from private initiative; construction cooperatives set up by trade associations can obtain low-interest credits to construct an industrial estate. In Senegal an industrial estate which promotes small and micro-enterprises is administered by the government agency SODIDA. This estate was opened in 1982 providing 20 workshops with offices. It now has 54. SODIDA provides economic and technical consultancy services, and financing for the purchase of raw materials. Administrative costs are recovered from rents, and enterprises are expanding and employment increasing. In Malaysia industrial estates have been established in various parts of the country.

Science parks aim to provide a physical, service and intellectual environment conducive to the creation and growth of advanced industries. Usually, parks are located close to a university or research institution which is expected to interact with industry. Often, the aim is to attract graduates from the educational institution to establish businesses or work in existing ones, and to attract branches of multinational companies which transfer technology and best practice into the region. It is quite common in the Netherlands for business incubators to be linked to science parks.

The first science parks were created in the United States and Japan. The idea then extended to Europe, with the Cambridge Science Park in the United Kingdom, the Berlin Centre for Innovation and New Enterprises in Germany, and the Sophia Antipolis Technopole near Antibes, France. Sweden has over ten science parks and Finland more than six. Norway's science parks are located in the main university towns, with other smaller parks attached to colleges in small towns. Denmark has several notable science parks, and by 1992 Germany had over 100, including 20 in the eastern part of the country.

The concept has spread to many other countries. Following the successful Dae Dok park in the Republic of Korea, other countries such as Malaysia, Singapore and Turkey have engaged in similar projects. In South America two dozen science parks are being established. In Africa there are plans for science parks in Senegal and Egypt, and in Central and Eastern Europe science parks are under construction in Hungary, Poland and Russia.

## 4. The aims and content of selected SME support programmes

### *Programmes to promote inter-enterprise linkages*

#### *Large-small enterprise linkages*

Opportunities for capacity building through the transfer of knowledge, technology and best practice between firms are increasing. Access to new markets, new technologies and new ideas depends as much on linkages with other firms as on support offered by institutions (Levy, 1994). For instance, access to international markets can depend more on linkages with private trading companies than on the activities of an official export agency. Equally, information on products and technologies is mainly obtained through connections with a major customer, or other small firms in the same industry. Therefore, the nature of relations between firms, and of the firms themselves, assumes key importance. Firms in international markets are an important source of information on competition at the world level. For this reason, support and service institutions must work closely with the private market, complementing and strengthening positive linkages, and redressing its failures.

It is clear that the source of competitive success lies beyond the confines of the single firm, and embraces many enterprises linked in a "value-adding chain". Pressure to cut costs, and to be more flexible, has led to de-integration, outsourcing and the use of subcontractors. Also, the rapid pace of innovation has strained the ability of individual firms to command the full range of innovations relevant to their operations. These developments, and current emphasis on quality, just-in-time delivery systems and computerized inter-firm linkages, have encouraged firms to focus on the calibre of their suppliers. In consequence, traditional patterns of inter-firm relationships are changing, as industrial sectors restructure.

As lead firms have identified their own success with that of their suppliers, conditions have become more conducive to inter-firm cooperation and to the tutoring of small firms towards world-class standards, although cases inevitably persist of small suppliers being unreasonably exploited by major customers.

In industrialized countries restructuring, specialization and a greater resort to subcontractors and suppliers are developing apace. In Japan contracting-out of

manufacturing and assembly is well established. Recent research at Tokyo university suggests that it now accounts for over a third of Japanese companies' total manufacturing costs and will increase to over 40 per cent by the end of the decade. In the 1960s it was less than 20 per cent (*Financial Times*, 16 March 1993).

Hitherto, large firms in developing countries have not tended to decentralize operations or to cooperate with suppliers and subcontractors. Moreover, where specialization and greater outsourcing does occur the motivation is often short-term lower costs and prices, and flexibility, rather than improving suppliers for long-term productive gain. Nevertheless, important changes are occurring. For example, in Mexico relations between shoe producers and their subcontractors have in the past been distant, with shoe manufacturers blaming suppliers for low quality and poor service, and suppliers blaming manufacturers for unstable demand, poor payment, and for focusing on price at the expense of quality. However, the importance of a systemic view of the production process, supported by strong collaboration, is now being recognized as critical to production of an internationally competitive product. Thus, in the city of León the associations of suppliers and footwear firms are working on fashion content and on the standardization of a measurement system (Rabellotti, 1994).

In Brazil, there is evidence of increased decentralization by large firms in the automobile industry, and of a trend towards helping small suppliers enhance their quality and productivity. Some large firms are reducing their first-tier suppliers and adopting supplier development programmes, in place of the practice of inviting bids on price for the same part. Supplier quality certification is an objective, and is seen as a necessary step to the transfer of internal production to subcontracting firms (Ruas et al., 1994).

In Indonesia subcontracting is very prevalent, but relationships between large and small firms are normally one-sided, with small firms often being dependent on them for access to markets, raw materials and capital. This has been the case, particularly in the batik industry, but less so in the footwear and textile sectors. The potential for the transfer of technology from large to small firms is strong but so far is only occurring sparingly (Smyth et al., 1994). In the food-processing sector in Kenya, the development of subcontracting linkages between large firms with small suppliers is not yet possible, mainly because of quality deficiencies. In India decentralization and subcontracting relations with small firms appear to be very prevalent, but here again small firms tend to be engaged in a one-sided relationship with large firms, with some significant exceptions (see box 4.5).

### *Strategies for maximizing skills and experience transfer among large and small enterprises*

Transfer of learning from large to small enterprises may be stimulated in various ways, including the review of proposals for investment in local supplier networks, financial incentives for subcontracting to small suppliers, and the establishment of subcontracting exchanges. Through tripartite agreements and guidelines, subcontracting practices can be brought to an accepted standard of fairness and mutual benefit.

**Box 4.5. Large firm/small firm linkages in India**

India is a developing country that is experiencing a rapid increase in outsourcing and in inter-firm subcontracting arrangements. In most cases, it seems, large firm/small firm relationships are not associated with a great deal of cooperation, and little learning occurs, with small-firm suppliers taking on a distant dependency role; in such cases relationships are "hands off", impersonal, hierarchical and relatively unpredictable.

However, there are cases of strong inter-firm vertical cooperation, with large firms and their suppliers forming long-term relationships, characterized by much transfer and sharing of technology and the raising of standards and learning among the suppliers, underpinned by a general ethos of trust and mutual accommodation. Maruti Udyog, a producer of cars and vans, and Punjab Tractors Limited have been identified as two such cases.

These firms have developed interdependent relationships with suppliers, relying heavily on smaller firms for components. This dependency has encouraged the "lead" firms to invest in the continuing health and efficiency of the whole industrial sector, helping suppliers to raise their technological capacities and levels of quality. For example, Maruti's engineers work with 45 key suppliers, conducting joint studies into their manufacturing processes, plant layout, administration and financing, and advising them on possible foreign and local technical collaboration. Its suppliers reported having learned greatly through this process of technology transfer.

The small firms that supply Punjab Tractors and Maruti are growing at a far higher rate than the suppliers of large Indian firms that do not promote cooperative development relationships.

Source: M. Tewari: *Sub-contracting relations in the age of flexibility* (Geneva, ILO, 1994).

In the Philippines government policies encourage subcontracting. Promotional policies have included the Tulong Sa Tao Subcontracting Financing Programme and the National Subcontractors' Exchange (SUBCONEX), a registry and placement service for subcontractors. There have also been mandatory local-content requirements for cars, motorcycles, trucks and electronic consumer goods. A priority concern of the Small and Medium-Sized Industries Development Organization, set up in Mauritius in 1993, is to strengthen linkages between small firms and larger firms located in the country's export processing zone, and to this end a Subcontracting Exchange Programme is being initiated (UNCTAD, 1995a).

Other attempts to induce large firm/small firm collaboration include the Network Programme in Norway. Under this programme, a large firm employing over 2,000 people was leader of a cooperative network of 11 small offshore oil and gas platforms. The managers from the large company recognize their dependency on small firms in the region. One of the organizational innovations is that departments in different firms together form standing committees on improving quality, joint purchasing, research and development, retraining, and marketing. This way, innovations are available to all member firms. Further networking takes place between the collaborating groups of firms, and supporting institutions such as technology institutes (Holmbeck, 1994).

The best way to forge links with large enterprises is to help small enterprises become attractive partners. Subcontracting exchanges only work well if the potential partners offer each other dynamic and innovative commercial opportunities. Therefore, policies to promote all sizes of enterprise need to strengthen the weakest links, having particular regard to local and sectoral conditions and priorities.

*Linkages among small enterprises*

Cooperation among small companies can be a very important vehicle for improving competitiveness and productivity by means of collective arrangements compensating for individual resource weaknesses. Cooperation between small firms helps to spread technical know-how, use economies of scale, and improve capacity to switch production processes and products with greater efficiency. This enhances the ability of an enterprise to tackle new kinds of work. Inter-firm cooperation can be in small groups of five or six enterprises, or in larger groups which come together to address a common need (such as credit, or access to specialized information) that can lead to other forms of cooperation.

In Uganda 3,000 shoeshiners began a savings and credit cooperative, but went on to equip each member with a standard desk, enhancing the image and acceptability of their trade. Their recent plans included a small unit to make shoe polish and brushes. In the United Republic of Tanzania a cluster of 527 micro-entrepreneurs and 395 trainees of various trades work on a common plot in the industrial area of Dar es Salaam. The cooperative organizes marketing and supplies for its members and owns several shops, through which members sell their products.

Under a nationwide initiative in Denmark, trained "brokers" help groups of small enterprises, typically five or six in number, to formulate joint ideas for cooperation in such areas as purchasing, production, marketing, and quality improvement. Together, the independent firms share costs and offer better services, taking large export orders from firms in neighbouring Germany. Initially, the cooperating group of firms receives a subsidy incentive, but after three years it must be entirely self-sustaining.

Similar initiatives have been taken in many countries. In Spain a group of cooperating businesses includes over 130 worker-owned enterprises, employing more than 26,000 worker-owners and expecting to employ 35,700 in 1996. In Canada 2,500 French-speaking Canadians in three isolated villages have established a savings and credit cooperative. This organization has led to a network of 16 consumer, handicraft and worker cooperatives employing nearly 350 people (Hansen, 1995).

The ILO has provided technical assistance in many developing countries. These include projects in Benin and Mali aimed at facilitating cooperation. The United Nations Industrial Development Organization (UNIDO) has supported initiatives in Guatemala, Honduras, Jamaica and Peru. In Kenya a project sponsored by the ILO and the TOOL Foundation (a Dutch NGO) helps small and micro-producers of agricultural and food-processing implements, inter alia, through entrepreneurial cooperation in sharing information and experience (see box 4.6). The Chilean Government has a programme to encourage small groups of SMEs to act collectively.



**Box 4.6. A subsector approach to enterprise promotion: The FIT programme**

FIT stands for "farm implements and tools", a reference to the focus of the programme on metalworkers, and particularly on their capacity to manufacture equipment for agriculture and food processing; the programme also aims to assist food processors. It is implemented by the ILO and the Dutch TOOL Foundation, through local partners, and has undertaken a number of pilot activities to enable the private sector to support small enterprises more effectively.

The clearly defined sectoral focus on metalworkers and food processors has enabled FIT and its local partners to gain considerable expertise and to become known by small enterprises active in those subsectors. Assistance can be provided in ways which are particularly appropriate, and concepts which prove to be valid for certain subsectors can also be relevant to others. FIT has found that farmers are very keen to meet small-scale metalworkers to explain the problems which they encounter with their implements, and to discuss possible solutions. After initial reluctance, metalworkers are finding that these meetings are also valuable for them. Though this particular producer-customer combination is unique, the principle of organizing such meetings has important implications for other subsectors.

As small enterprises begin to expand, they are keen to develop their own entrepreneurial networks, for example through visits to other small enterprises, and have indicated a strong preference for visiting enterprises in the same (or at least, closely related) subsectors. When enabled to do this, they exchange a wide range of commercially valuable information in a short time about improved sources of raw materials, product designs, management skills, and so on. Similarly, large enterprises are interested in establishing dialogue with the more promising SMEs in related subsectors, bearing in mind potential future linkages (with a few exceptions, such as bakeries, where SMEs can pose a threat).

This need to connect with enterprises in related subsectors is one which many SMEs feel quite acutely, to the point where they are often willing to pay all of the direct costs if an external agency can simply facilitate contact. This is true nationally and regionally; enterprises with connections abroad are often seen to enjoy a competitive advantage over other SMEs. A sectoral focus enables FIT to satisfy this need to develop a web of commercial connections, which ultimately spans many countries.

Cooperating groups need access to many support services. Increasingly, they receive these from dedicated institutions — such as common facilities and business development centres, training centres, and credit agencies — that can provide enterprise-specific services (see box 4.7).

*Sectoral programmes for SME promotion*

Advisory and support programmes to small enterprises focus increasingly on sector-specific requirements. In a constantly changing competitive environment, individual small firms can be hampered by slow and inefficient suppliers, and can lose

**Box 4.7. Colombia: Institutional support for small firm cooperative groups**

Sixteen small footwear enterprises in Bucaramanga, in north-eastern Colombia, have grouped together to fund the purchase of land and the construction of interconnected buildings to house all 16 independently owned businesses and a modern technology centre to train workers in leather production and provide technology services to the industry. This building constellation and the group who occupy it are known as the Cooperative Footwear Industry Centre (ASOCALZA, Asociación Ciudadela Industrial del Calzaldo).

The 16 enterprises decided they could improve their productivity, quality and export performance by acting together, whilst continuing to remain independent. Consequently, they began to share customers, machinery, raw materials (especially leather), skills and experience, the object being to learn and improve continuously. Regular experience-sharing meetings are held and entrepreneurs inspect one another's workshops. They also share orders, and some of the new workshops are connected by sliding doors so that big orders can be met by sliding them back to make a larger factory.

Within just four years the small firms have come to employ close to 1,000 people at peak times and have become export-oriented with modern technology and premises. They retain a social and institutional arrangement (including the technology centre) that facilitates new ideas and constant improvement.

Source: L. E. Romero et al.: *Bridging the gap between handicrafts and industry: The cooperative footwear industrial centre in Bucaramanga, Colombia* (Bogotá, Universidad de Los Andes, 1992).

out to competitors and distributors in the same sector. The new emphasis is on flexibility, quality, speed, productivity, and innovation. This gives a competitive edge to enterprises that rely on the strong capabilities of others in the sector. Action can be targeted on national sectors, such as footwear or clothing, or on local sectors, possibly based in small-firm industrial districts.

Policy-makers also take into account the international dimension: how local industry fits into global patterns, and the strategies required to gain access to international markets, or attract quality enterprises. Therefore, programmes are being developed which assess the support needs of specific sectors, based on consultation and participation of employers' and workers' representatives.

In Côte d'Ivoire the ILO has helped to strengthen services to entrepreneurs producing and using local building materials. Following an analysis of needs, a package of services was arranged, including vocational training, standards and specifications for local building materials, a certification scheme (including the right to use a quality label), production of good, affordable local equipment, marketing policies, and advice on improving working conditions and on safety and health in the workplace. This has led to an increase in both the number of small enterprises and the use of local building materials.

Another ILO project has enhanced the skills, productivity and overall performance of small and medium-sized enterprises in the food-processing sector in

the Asia-Pacific region. Its sectoral focus made it possible to address detailed and specific needs. Managerial and technical consultancy services, including training courses, were provided for 81 enterprises, with a focus on productivity concepts and technologies. Also, the capacity of support institutions to provide advisory services to small and medium-sized enterprises was strengthened. The project was successful, led to measurable improvements in productivity and an improved work environment, and is an important demonstration model.

Small and medium-sized enterprises, which often employ as much as 25 per cent of the rural workforce in developing countries, can help to overcome the frequently endemic problems of unemployment and underemployment, and to stem migration to overcrowded urban areas. Typically, these enterprises employ only a few, often family, workers, and individual artisans. Along with rural cooperatives and cottage workers, they engage in handicraft and small-scale manufacturing, repair services and small-scale contracting. Often they are agro-related, and the dominant sectors therefore include food processing, beverages, textile spinning and weaving, garments, tanning and leatherwork, carpentry, furniture-making, and metal fabrication for the production of basic tools and implements. Characteristically, they are widely dispersed and use simple, labour-intensive technology.

The promotion of small rural enterprises needs to reflect the wider economic environment in which they operate. For instance, policies to promote high agricultural growth rates and incomes create an effective demand for local products and services, a critical prerequisite for firms relying on immediate local markets. Also, policies concerned with infrastructure and social services in rural areas, favourable terms of trade for farmers, investment in agricultural extension and research, and the provision of credit for farmers all have an impact on the success of small rural enterprises.

Support services in marketing and raw material supply can be effective in rural areas if aimed at stimulating private enterprises or cooperatives to perform these functions. Other support services, such as credit, training, extension and technical assistance, are effective when decentralized and on-site, which means that mobility of extension services is crucial. In small towns trade associations perform an effective role in delivering services. Private voluntary organizations and NGOs are particularly effective in rural areas, since they draw on the strengths of autonomous local operations and have a grass-roots orientation. Programmes that have proved successful have ensured strong local community involvement in the design and implementation of programmes.

### *Franchising*

Franchising combines many of the advantages of a large business (such as economies of scale in purchasing, advertising, product development, experience and expertise) with some of the advantages of small-scale entrepreneurship (such as a high level of commitment and motivation, and local contacts and knowledge). In the United States, franchised businesses account for around 80 per cent of new businesses in the retail sector.

The increasing expansion of business through franchising reflects the considerable advantages to both the franchiser and the franchisee. Under this arrangement the owner of a proven business concept, the franchiser, grants an "entrepreneur" the right by contract to establish a similar business. In exchange for

franchise fees and the obligation to adhere to strict quality standards, the acquires the right to use the franchiser's trademark, and receives marketi detailed manuals on how to operate the business, start-up assistance, sta collective equipment, raw materials procurement facilities and, often assistance.

This arrangement considerably reduces the risks of entrepreneurship. every new business developing the basic business concept and designing facilities and control systems, the franchise set-up offers a tested and prov This allows the entrepreneur to dedicate energy to the day-to-day runn business, and avoid the pitfalls which account for many small busine Whether or not the franchisee is regarded as an entrepreneur, small bus started and employment created. Also, the standardized approach tends maintenance of good standards and working conditions.

Because franchising can create large numbers of quality jobs, the ILO with governments in several Asian countries to implement programmes fo promotion. These include creating systems to identify local small-scal successes which have the potential for replication through franchising. have been identified, and the owner has decided to become a franchiser, a provided through a franchise resource centre to assist in developing t franchise concept, field-test prototype operations, develop operations manu financing, analyse locations, and take other steps to develop a successfu operation (Henriques, 1995b).

### *Programmes to assist internationalization*

With increasing economic globalization, it is important for smal internationalize so as to gain access to markets and suppliers in other coun small firms are in a position to sell directly on foreign markets on an indivi invest in other small firms as subcontractors or join foreign joint ventures to new markets, but in most cases their limited resources place them at a dis Various strategies exist to overcome this drawback:

— Small firms may join together in a consortium to market their products share the costs, and share the profits. Small firms which are direct comp it more difficult to cooperate than those which see themselves as comp but even direct competitors have cooperated in specific markets, or i such as sharing the costs of attending a trade fair.

— Trade associations are generally larger than consortia and include comp non-competitors. On behalf of their members, they provide services internationalization. For example, the export-oriented small and me packaging machine manufacturers of Italy have a trade association v targeting export markets in several parts of the world.

— Increasingly, small firms are being given access to business oppor computerized information networks. The European Union, for exampl such a service, as does UNCTAD through its Global Trade Point N

— Small firms can gain access to international markets by acting as s subcontractors to local branches of large multinational manufacturers companies. Or local small firms can sell to other local firms whi

themselves multinationals but have contracts with multinational distributors. For example, shoes are sold in Western markets by multinationals that have sourced their products worldwide, often dealing with key local assemblers through their own local subcontractors.

— Many small firms use trading companies or agents, often based in other countries, which sell the products of a range of enterprises.

— Many international buyers approach manufacturers directly, especially when small enterprises are grouped in agglomerations or industrial districts with an international reputation for supplying a wide range of a particular product (jewellery, garments, leatherwork).

### *Programmes of interregional cooperation*

A further means of advancing internationalization is to link small and medium-sized enterprises through international institutions, or national agencies with international connections (see box 4.8). Some donor programmes help to promote inter-firm linkages between domestic firms and developing countries. One example is the Indo-German Export Promotion Project, supported by GTZ, the German technical cooperation agency, which aims to build relationships between Indian and German firms (UNCTAD, 1995c). A recent development has been to build up links with other countries to facilitate international business.

**Box 4.8. The Steinbeis Foundation: Linking up small-firm support institutions in different countries**

The Steinbeis Foundation specializes in transferring technology to small and medium-sized firms in Baden-Wurttemberg, in Germany, through its large network of transfer centres.

The Foundation is now also transferring the know-how about how to set up a national or regional technology transfer system. The objective is to design and implement a technology transfer model adapted to the existing infrastructure of the country in question, but based on the same principles as the Steinbeis Foundation itself. For example, in June 1994 an agreement was signed with a Chilean partner foundation, the Fundación Chile, to help it develop its own technology transfer system. The ultimate objective is to raise the value added in the partner country and help those involved to help themselves. In addition, the process is intended to strengthen economic cooperation between small companies in Chile and enterprises in Baden-Wurttemberg. While Chile's own market is attractive, the country also has the potential for acting as a stepping stone to the rest of the Latin American region. Similar projects are currently under way in Finland, India, Norway, South Africa, Thailand and other countries.

Source: Steinbeis Foundation: *Annual Report* (Stuttgart, Steinbeis Foundation for Economic Promotion, 1994).

The leading Brazilian SME support institution, SEBRAE, is building up links in the MERCOSUR region so as to provide its services to small exporters and importers, as well as bring them together within the region. Also, the United Nations EMPRETEC programme, which detects entrepreneurial talent and fosters its development, has pioneered networking and business links between Africa and Latin America (UNCTAD, 1995c). With the support of the European Union's PHARE programme, 14 regional development agencies have been established in Bulgaria, Czech Republic, Hungary, Poland and Slovakia. They link up local small and medium-sized enterprises to activities in different regions and across national borders (Mirel and Thompson, 1994).

Some consumer cooperatives in developed countries have established links with communities of indigenous peoples to promote the sale of traditional medicinal and other plants which they cultivate. The ILO's INTERCOOP programme brings cooperative enterprises in various parts of the world into contact with one another, and with other enterprises, as trading partners.

### *Programmes to improve working conditions and productivity*

An important ILO initiative is the Work Improvements in Small Enterprises (WISE) programme. The experience of this programme has been that relatively low-cost improvements in working conditions such as lighting, safety and alleviation of stress have resulted in improvements in quality, productivity and competitiveness in all sizes of firms (see box 4.9).

### *Programmes to promote social protection in small and medium-sized enterprises*

Social protection for workers in small and medium-sized enterprises, and their families, can be provided by:

- extension of social security to unprotected sectors: this requires removal of ceilings or thresholds limiting the coverage of social protection schemes. For example, in India, it was decided in 1995 to raise the contribution ceiling for benefits provided by the Employee State Insurance Corporation (health care, employment injury, sickness and maternity benefits). In addition, there are plans to lower the threshold for eligibility to the Employees Provident Fund from enterprises with more than 20 employees to those with more than ten employees; this is likely to increase the coverage from 17 to 25 million workers;
- improving and extending social assistance: many developing countries have set up social assistance schemes that benefit retired workers from small and medium-sized enterprises and their families. For example, in Mongolia local Assistance Councils provide winter clothing and boots for children who would otherwise not be able to go to school, and also free lunches, discount rents and fuel costs for the disabled and elderly who have no family support or have not been able to insure themselves during their working lives;
- promoting self-help schemes for social insurance: in many developing countries workers and the self-employed have organized self-help schemes, often tied to associations providing other benefits. Some groups are set up specifically to

**Box 4.9. United Republic of Tanzania: Improving competitiveness through better working conditions**

Six small and medium-sized factories in the United Republic of Tanzania received assistance from the ILO's WISE programme in raising productivity, quality and competitiveness through improvements in working conditions. Several months later follow-up evaluations were carried out through interviews with managers and workers and all concluded that significant improvements had been made all round. Three examples are briefly described below.

A first evaluation asked 21 workers in an enterprise employing 46 people that made paper products what effect improvements in lighting had on their work performance. Sixty-six per cent said that their working speed had improved, 71 per cent that their output had risen, and 81 per cent that they had been able to improve the quality of their work. At the same time, 100 per cent said that they had become aware of an improvement in their working conditions, with over a third saying they were much better; 90 per cent felt safety had improved and 86 per cent reported more job satisfaction.

A second evaluation asked a factory manager of a small plant of 25 workers making wooden furniture what had been the benefits of reorganizing storage facilities for raw wood material that had previously lain around the workshop floor causing accidents and back pains caused by continual bending. "Remarkable savings" in time (and money) were reported, and additional (expensive) floor space was freed. This has been accompanied by a significant reduction in accidents. Interviews with ten workers produced unanimous responses that working conditions, safety and job satisfaction had all improved.

A third evaluation concerned a small factory of 35 employees making aluminium kitchenware. Low-cost improvements (costing approximately $100) were made to heating, humidity control and lighting. A follow-up interview with the factory manager revealed that the company had made "remarkable savings through the reduction in time waste", quality had improved, and there had been considerable increases in output and profits. Interviews with ten workers revealed that all were agreed that working conditions, safety and job satisfaction had improved; and they confirmed that a consequence was "much better" work performance in terms of output, speed and quality.

Source: ILO: *WISE follow-up case-study*, Working Conditions and Environment Department (Geneva, 1995).

provide social protection for members. Examples of these are "village pharmacies" in Niger, housing cooperatives in Egypt, and the mutual insurance organizations operating in most European countries. Often, associations established for business reasons extend their services into the social protection sphere. In Zaire an association of wheelbarrow drivers is active in Kinshasa (with 30,000 members) and Lubumbashi (with 20,000 members). This association was originally a form of trade union which negotiated standard terms between wheelbarrow owners and drivers. Now, it has also organized social services such as life insurance (for drivers killed in traffic), a primary school, and primary health care.

In India the Self-Employed Women's Association (SEWA) in Ahmedabad offers a range of benefits in the event of death, hospitalization or damage to houses and some production assets. About 7,000 women members are covered. In the United Republic of Tanzania about 1,000 market vendors of the Mwanayamala cooperative in Dar es Salaam pay a daily rate of Tsh.20-30 for renting the space of their stands. These contributions finance items like funeral costs and hospital treatment. In El Salvador about 1,000 vendors of the Central Municipal Market in San Salvador contribute to a health fund that reimburses some health and hospitalization costs for members and their families. Some voluntary social service systems are established with the help of employers who understand the value of maintaining the stability of the workforce.

### *Programmes for women entrepreneurs*

There are a number of gender-specific constraints to setting up and operating enterprises. These include:

- role barriers, where there are conflicting role demands and time constraints, such as may occur where women have primary responsibility for raising children;
- social and cultural barriers, such as negative attitudes towards women in business, the fact that women are supposed to fulfil other roles, restrictions as to the choice of sector, lack of family support, and lack of mobility;
- educational barriers, where women have relatively lower education levels, may have received a biased education and usually have limited access to vocational training opportunities;
- occupational barriers, inasmuch as women generally have fewer opportunities in the formal sector for skill development;
- infrastructural barriers, such as insufficient access to credit, technology, support services, land and information, which can be particularly acute for women;
- legal barriers, resulting in a situation where independent legal action is difficult for women;
- behavioural barriers, inasmuch as women may have little self-confidence and a negative self-image.

Given these barriers, there is a need to supplement the regulatory and institutional policies described in this report with special programmes to promote female entrepreneurship in small and micro-enterprises, and to ensure that more general programmes address specific gender issues.

The creation of a service infrastructure should pay attention to the barriers and constraints faced by women in taking advantage of what is on offer. For example, low-income women normally are busy and less mobile than men. Consequently, it is important that services, such as lending and savings services, are available where the women are located. Moreover, the regulatory burdens on women, such as constraints on property rights and the legal barriers to women's access to credit, need to be eased.

Many countries have programmes and institutions catering for the specific needs of women entrepreneurs. In Botswana the Women's Finance House targets women

who are small and micro-entrepreneurs in and around Gaborone. Its main activities are the operating of credit and savings programmes and the provision of training for women interested in starting their own business (Women's World Banking, 1994). In Kenya, there are about 40 NGOs providing support services to women workers in the rural and informal sectors, through specific programmes targeted at women's groups or individual women entrepreneurs (ILO, 1995c).

In South America organizations like the Brazilian Association for the Development of Women and the Bolivian Foundation for the Development of Women, provide women micro-entrepreneurs with credit, carry out training courses, and (in the case of the Brazilian institution) provide technical cooperation in such areas as quality improvement, as well as advice on legal matters (Women's World Banking, 1994).

Of the countries in transition, Poland has a number of support institutions and programmes tailored to the needs of women workers and entrepreneurs. These include the Centre for the Advancement of Women which, located in Warsaw, acts as a quasi-employment agency, carries out research on women's labour market issues, provides information on the activities of other women's groups in Poland, and provides training courses. The Foundation for the Development of Polish Agriculture (FDPA) has, among other things, supported the Women in Rural Enterprise Development Programme (WIRED), which provides training and finance for rural women. This programme, established to address the particular needs of rural women, offers training in business management and finance, accompanied by self-awareness training and positive-thinking seminars. Upon completion of courses graduates can form groups which can apply for financial assistance from the programme's revolving fund. Another significant development is the attention now being given to Poland's 36,000 rural women's circles in respect of the creation of women-owned small and medium-sized enterprises (GEMINI, 1994).

Internationally, a well-known organization catering specifically for female small-scale entrepreneurs is Women's World Banking (WWB), which has affiliates in many countries. The ILO has also been extensively involved in programmes to promote women entrepreneurship through research, technical cooperation and advisory services. An integrated approach is generally used, providing assistance on several fronts simultaneously: credit, technology, training, management, marketing and organization. An ongoing ILO project promotes the organization of women working in Benin's food-processing and street-food trade and is identifying possible new activities for women entrepreneurs.

### *Special programmes*

Some groups and people in particularly difficult socio-economic circumstances, require special measures to encourage entrepreneurial development. They include workers in the informal sector and their dependents, indigenous and tribal peoples, the disabled and people in countries affected by war.

#### *Informal sector*

The very small-scale informal sector faces even greater development challenges than other small enterprises. Technological and productivity levels are likely to be

low, access to markets limited, and the resource base weak. Many support services aimed at small enterprises cater to the informal sector, enabling informal enterprises to benefit from special credit programmes and simplified administrative procedures. The availability of physical facilities can improve operations and provide a good environment for gaining access to credit and acquiring assets. Ecuador has an incentive scheme under which registration entitles micro-enterprises credit facilities and other benefits. Various practical training and advisory programmes provide the skills needed for growth and development. The informal sector's contribution to job creation and social welfare is also sustained by improvements in general education and the promotion of an enterprise culture.

A national informal sector policy, aimed at reducing the constraints faced by the sector and promoting its growth, has recently been introduced with ILO assistance in the United Republic of Tanzania. The focus has been on helping micro-enterprises to help themselves and providing members with such services as credit and savings schemes and social protection arrangements.

Other recent ILO action in Colombia and the Philippines has combined improvements in working conditions and social protection with technical assistance to improve productivity and gain access to new markets. In the long term, in line with the Director-General's 1991 Report, *The dilemma of the informal sector*, full integration into the organized sector will remain the objective.

### *Indigenous and tribal peoples*

Indigenous and tribal peoples constitute the largest identifiable minority groups on earth, with a total of more than 300 million people. They face social, cultural and, in some cases, legal constraints which often are aggravated by geographical isolation. Consequently, special development programmes are needed.

The ILO has adopted the only two existing international Conventions on indigenous and tribal peoples, which were drawn up in close cooperation with the United Nations. The Indigenous and Tribal Populations Convention, 1957 (No. 107), marked the first ever attempt to codify the rights of these peoples. The Indigenous and Tribal Peoples Convention, 1989 (No. 169), recognizes the aspirations of these peoples to exercise control over their own institutions, languages and religions as well as their rights to manage their territories, natural resources and the environment. It also calls for recognition of the fundamental human rights of indigenous and tribal peoples within the nation in which they live. Article 23 of Convention No. 169 indicates that "handicrafts, rural and community-based industries, and subsistence economy and traditional activities of the peoples concerned, such as hunting, fishing, trapping and gathering, shall be recognized as important factors in the maintenance of their cultures and in their economic self-reliance and development".

The ILO's INDISCO programme is a practical response to Convention No. 169. It aims at assisting indigenous and tribal peoples in promoting their own systems for employment and income generation, safeguarding their traditional values, knowledge and practices, and strengthening their traditional institutions with support mechanisms such as cooperatives, self-help organizations and small enterprises. Since April 1994 the programme has implemented nine pilot projects in India and the Philippines, in close cooperation with selected indigenous and tribal communities and their NGOs. Alternative employment avenues have been created for 4,500 tribal

families in India and about 2,000 indigenous families in the Philippines through the establishment of informal self-help organizations, multi-purpose cooperative societies and small enterprises in areas such as traditional farming, fishing, handicraft production and marketing, livestock breeding, weaving, and the collection and sale of minor forest produce. Small enterprises established by the indigenous and tribal peoples are supported by training and advisory services offered by extension workers, and through credit provided by community-based revolving loan funds. The INDISCO programme is finalizing pilot projects for indigenous and tribal communities in West Africa and Central America.

*Disabled*

Self-employment in small and micro-enterprises, and employment in cooperatives, workshops and associative enterprises, are viable options for some disabled individuals. There are many examples of successful disabled entrepreneurs, both individuals and groups, in industrialized and developing countries and in countries in transition. Their need for business management skills, advisory services, access to new technologies, credit and markets, as well as for a supportive policy and regulatory environment, is the same as for non-disabled entrepreneurs. However, some disabled individuals require special measures to enable them to maximize their capacity and to compete successfully.

Such special measures are of two categories: those determined by, and addressing the special needs of, the individual, and those necessary to create favourable conditions for the full participation of disabled persons in society in general, and in small and micro-enterprises specifically. Examples of the first category include the adaptation of training and equipment to individual needs — for example, computer keyboards in Braille and voice outputs for blind and visually impaired persons, the use of sign language for communication with deaf and hearing-impaired persons, and the modification of worksite premises and facilities to make them accessible to mobility-impaired persons, such as wheelchair users. Other special measures include the provision of personal technical aids and devices, remedial education to enable disabled individuals to enter training courses, and social competency and confidence building exercises.

Examples of the second category of special measures include the granting of tax benefits for enterprises that employ disabled workers, awarding government contracts to enterprises run by disabled persons and providing subsidies to self-help production workshops operated by disabled individuals. Due to negative public attitudes and practices towards disabled persons, special public media and other efforts are sometimes required to create favourable conditions for the successful operation of business enterprises by disabled persons. The adoption of legislation prohibiting discrimination against disabled persons may also be required.

Major technical and financial support to disabled individuals and groups engaged in small and micro-enterprise activities has been provided by the ILO and other organizations, particularly in developing countries, by way of special projects exclusively targeting disabled persons. Such special projects have often been implemented by, or in collaboration with, governments, NGOs and national or local associations of disabled persons. The projects have typically provided business skills training, credit, marketing assistance, and other services (see box 4.10).

**Box 4.10. ILO projects to assist disabled entrepreneurs**

In Kenya, with ILO assistance, a Disabled Persons Loan Scheme was established. This scheme provided, to specially selected disabled entrepreneurs in 20 districts, business skills training and business advisory services by small and medium enterprise development NGOs, and commercial loans from Barclays Bank of Kenya Limited backed by a loan guarantee fund. Over 1,000 disabled individuals received training, and 263 received loans for their businesses.

In another approach, in Nigeria, a committee was formed of interested local government officials, parents, disabled persons, rehabilitation service providers and business persons in the city of Ibadan, to identify and raise funds for on-the-job or apprentice training for selected disabled persons in the community.

The committee has arranged for 30 disabled women and men to be trained locally in activities such as poultry-keeping, weaving, food preparation, soap-making, shoemaking and repair, typing and radio repair, and has assisted them to start their own activities, sometimes with parental financial support. Most have also received a small loan from a revolving loan fund established with the People's Bank of Nigeria.

A third example relates to an attempt in Dar es Salaam to strengthen the capacity of the national organizations of disabled persons to influence policy and to include selected disabled informal-sector entrepreneurs as beneficiaries of the general services provided to non-disabled people.

However, because they often lack the organizational strength, technical capability and financial resources for such special programmes, government agencies, NGOs and associations of disabled persons are increasingly turning to general small-enterprise development organizations and programmes for help. Where this occurs, the provision of special measures as described above is not the responsibility of the programmes themselves. If a disabled individual requires a technical aid or remedial education to participate in an SME programme, a referral to an appropriate agency should be made, with a view to later admittance into the programme. However, SME programmes must ensure that their services are accessible to disabled individuals. In addition, programme staff should be knowledgeable about the needs of individuals with different types of disabilities and be able to propose common-sense solutions to problems encountered by disabled persons in operating their businesses.

*War-affected countries*

Armed conflict has affected a large number of countries in recent years, many of which were at a low level of economic, social and human development even prior to the conflict, which then caused further rapid and serious deterioration. One of the key challenges facing these countries is that of reconstruction and rehabilitation. A particularly important issue in this respect is the creation of employment for the large numbers of war-affected people such as refugees, internally displaced persons, and

demilitarized personnel. One key action can be a concerted effort to promote small and medium-sized enterprises, which can contribute significantly to employment generation, economic growth and empowerment of the large number of persons who are disadvantaged in social and economic terms because of the war situation.

The ILO has provided technical assistance in designing and implementing SME support programmes in Angola, Cambodia and Mozambique (see box 4.11). Experience indicates that such efforts need to consider a number of special characteristics of war-affected countries, including: low economic growth and low per capita income; a narrow industrial base; shortage of capital; the need for structural adjustment and economic reform; and high inflation. In countries affected by armed conflict, the effect of these factors becomes more pronounced. In addition, their economic difficulties are often exacerbated by an uncertain political environment, a breakdown or destruction of economic and social infrastructures, a weakness in inputs, markets and institutions, and demographic and social factors. These special circumstances mean that support activities must allow for constraints such as the insecurity or inaccessibility of a project area, an unstable social situation, and frequent, unpredictable population movements.

In respect of target groups for small and medium enterprise programmes, it is not usually either feasible or desirable to focus narrowly on ex-combatants. Rather, programmes should aim at assisting a wider group of war-affected groups, such as internally displaced persons, returning refugees and others in need. A narrow definition of the target group can create problems of equity and logistics (too dispersed a target population) and reinforce existing social divisions.

It is also crucial to undertake surveys of the intended target group (demilitarized personnel, returning refugees, internally displaced persons) to ascertain their skill profiles, employment intentions, and settlement patterns. Since there is often a lack of feasible business ideas, it is important to conduct business opportunity identification surveys to guide subsequent programme design and training activities. Most programmes will need to combine basic business start-up and management training with vocational training, as well as provide credit access, tool kits, follow-up support and other inputs.

At the programme formulation stage, changes should be foreseen regarding the approach, content, target group, area of concentration and size of the programme. Experience in Cambodia and Mozambique indicates that as overall planning for the reintegration of demobilized combatants and other conflict-affected groups makes progress, the nature of the programme components may change. This could be due to several reasons: changes in overall priorities, political negotiations between parties to the conflict, delays in demobilization (Cambodia), scaling down of programmes, reallocation of resources, etc. Considerable flexibility is therefore required in project formulation. One approach is to divide the project into two or more phases, with the first phase (core component) limited in time (two to three years as in Cambodia) or in coverage (first group of 4,000 demobilized combatants as in Mozambique, or five districts as in Cambodia) and a second phase (expansion component) to be undertaken should funding be available. This approach also greatly facilitates the integration of special or targeted programmes into the longer-term national reconstruction programme.

With regard to delivery mechanisms it is important to rely extensively on a decentralized approach which utilizes NGO resources and other self-help structures.

**Box 4.11. Cambodia: Small-scale business activities to help a war-torn country**

The ILO is supporting the establishment and implementation of a programme to promote small-scale activities in the private sector in Cambodia. The programme is delivered through five Local Economic Development Agencies (LEDAs) located in Phnom Penh, Battambang, Sisophon, Siem Reap and Kompong Cham.

The LEDAs provide services for the establishment of new businesses and the expansion of existing businesses, as well as for increasing the earnings of the self-employed in the urban informal sector. The services consist of:

- business opportunity identification;
- training in entrepreneurship and small business management;
- credit, including micro-credit provided to groups of self-employed women;
- business counselling and marketing advice;
- referral to skills training programmes.

Business opportunity surveys are used to design training programmes for small enterprise promotion, which each LEDA now runs on a monthly basis. Follow-up services are being provided to assist trainees to complete their business plans and loan applications, and credit is being disbursed. Fifty per cent of the participants are women. The project also has a special component to assist disabled entrepreneurs who constitute a particularly large group in the population.

Often government structures are severely affected by the conflict in terms of human and physical resources, and can also be politically aligned with one particular faction. These factors may make government institutions less suitable than more neutral alternatives.

### 5. Need for overall coordination of SME programmes

Harmonization of fragmented regulations, programmes and institutions is key to the support of small and medium-sized enterprises. Fragmentation can occur at the local or national level, and also between local, national (and increasingly) supranational levels, as in enlarged market areas such as the European Union and MERCOSUR. Policies affecting small and medium-sized enterprises may involve government departments dealing with issues ranging from social protection to industrial promotion, export promotion or training. Within the private sector there can be many changing players, including chambers of commerce, trade associations and consultants. There also are many NGOs with independent programmes, and many international donor programmes and agencies. The challenge is how to make best use of all these initiatives so that they mutually support and reinforce small and medium enterprise development, rather than inhibit or stifle it.

Increasingly, coordination committees, donor committees and tripartite consensus-forming committees are developing to address this problem. Apex

institutions are also emerging to harmonize the activities and networks of regional and local institutions. For example, the Portuguese Institute for the Support of Small and Medium-Sized Enterprises and Investment (IAPME) is a semi-autonomous apex body, formally responsible to three ministries (Trade, Industry and Finance). Its structure includes a consultative body of employers, trade unions and professional associations. IAPME has its head office in Lisbon, and has three regional offices in major towns to coordinate smaller regional offices. IAPME coordinates policies for small and medium-sized enterprises, aimed at improving managerial capabilities, modernizing enterprise structures, and providing institutional support, including the encouragement of inter-firm cooperation. Similar semi-autonomous apex institutions established to support small business include those in Spain (IMPI), Greece (EOMMEX) and Italy (IMPI) and, at a more localized level, in Valencia, Spain (IMPIVA), and Emilia Romagna, Italy (ERVET).

There are similar institutions in Mozambique (IDIL) and Angola (INAPEM). In Brazil, the Centre for the Support of Small and Medium-Sized Enterprises (SEBRAE), with its regional and local support centres, is the principal institution implementing policies aimed at small and medium-sized firms. Among other activities, SEBRAE promotes research and human resource development, provides technical assistance and, in particular, disseminates information through a large countrywide network of centres (Alexim, 1993).

In Turkey, the Small and Medium-Sized Industry Development Organization (SMIDO) was established in 1990 to help small and medium-sized firms by facilitating: the establishment of technology centres, technoparks, consultancy centres and similar institutes for research and development; the promotion of information dissemination; the establishment of development centres to provide support programmes on such matters as modernization, management, marketing, and technological adaptation; and the establishment of technical training centres. So far SMIDO has established 13 consultancy and development centres, two technoparks and two technical training centres (UNCTAD, 1995a).

In South Africa the Government is creating an apex body responsible for a range of SME promotion activities, which will include a special unit to coordinate a key element of small and medium enterprise strategy, namely, a nationwide network of local service centres (LSCs) to support small and micro-enterprises and of regional manufacturing technology centres (RMTCs) to support small manufacturing enterprises. On completion, the network will be capable of offering a full spectrum of support in a fashion which reflects local economic characteristics. The LSCs are owned and driven by key stakeholders and meet agreed quality standards and performance benchmarks. Basically, the network will be self-regulating, with the Government playing the role of catalyst, enabler and facilitator rather than seeking to exercise autocratic control. A crucial object of the LSCs and RMTCs is that they should network and collaborate with other organizations, including local government, community organizations, financial institutions, professional associations, consulting firms, law firms and others. The coordinating unit, to be known as the LSC Development Unit, will assist the LSCs and RMTCs to network, to identify needs for new LSCs, to provide additional services where gaps appear, and to accredit and evaluate the performance of LSCs.

As to the transition economies, the Foundation for Enterprise Promotion in Hungary is an apex institution that is facilitating the development of 19 local

enterprise agencies and 120 SME information and counselling centres across the country, as well as supporting other development institutions and programmes ranging from the provision of training to the financing of small and medium enterprise research. The local enterprise agencies have been given a wide brief which includes coordination of other agencies acting at the local level. The individual local enterprise agencies differ according to the needs of their particular location, but activities typically include the provision of information, the production of business plans, the training of new entrepreneurs, and support in connection with regional development issues (Burns, 1995; and Mirel and Thompson, 1994).

In Lithuania a national Small and Medium Enterprise Development Agency with a broad range of responsibilities for small firm promotion is being established. Similar semi-autonomous dedicated institutions responsible for implementing SME programmes have been established in Albania, Czech Republic, Estonia, Latvia and Slovakia (Mirel and Thompson, 1994).

Poland also has recently established a quasi-government apex institution called the Polish Foundation for the Promotion and Development of Small and Medium Enterprises. This will be the key agency for supporting and developing the Polish SME sector, with the mission of upgrading small and medium enterprise competitiveness. The policy-making body of the Foundation is a supervisory council chaired by a representative of the Ministry of Industry and Trade, with other members representing three other ministries and seven non-governmental organizations, including business associations, financial institutions and regional development agencies. Furthermore, there is consultation with local, regional and national organizations that either represent the SME sector or provide services to it. The Foundation's programmes are developed in consultation with, and implemented through, these organizations. Programmes to support small and medium-sized enterprises include: improvements in legal and fiscal regulations; the provision of access to training, information on marketing, technology, aid programmes and other matters; access to finance; and the development of physical facilities, including business incubators.

The highly developed and coordinated programme of support for small and medium-sized enterprises in Poland contrasts sharply with the situation in Uzbekistan, where it was recently reported that the country lacked a coherent national policy or framework for SME development (S. White and J. Petterson, 1995). In Belarus small and medium enterprise policy is said to be hampered by a lack of coordination of activities to promote small firms emanating from a number of government ministries. There is a need for harnessing and directing the various activities towards agreed common goals. Currently, the creation of an apex coordinating body is under discussion, along with the development of an overall SME strategy for Belarus, possibly incorporating a regional dimension (Merkulov, 1995). The need for greater networking and harmonization among the fast growing number of SME support agencies is also at the forefront of policy-makers' minds in Romania, whose local SME development centres are being integrated into a decentralized national support network. Initially, the local centres will offer consultancy and information services, but eventually they are expected to act as local development agencies (UNCTAD, 1995a).

## CHAPTER V

## INTERNATIONAL LABOUR STANDARDS AND SMES

A large number of existing standards, including many dealing with basic human rights, are applicable to all workers, whatever the size of enterprise that employs them. However, there are a number of standards that make specific reference to small enterprises.

### *Specific arrangements*

Two instruments take into account possible difficulties in their application to small enterprises by providing for specific arrangements. The Occupational Safety and Health Recommendation, 1981 (No. 164), indicates the organizational measures for which employers could be made responsible; the Asbestos Recommendation, 1986 (No. 172), provides that the competent authority should undertake activities to assist small enterprises where technical knowledge or means may be lacking, with the establishment of preventive programmes in cases where exposure to asbestos could occur.

### *Flexibility clauses*

There are also instruments which recognize small firms by authorizing certain exclusions or exceptions. Flexibility clauses in respect of scope included in some Conventions give the ratifying State the possibility of limiting its obligations depending on the size of the enterprise. States party to the Employment Promotion and Protection against Unemployment Convention, 1988 (No. 168), may choose, where specifically justified by the level of development, to protect prescribed classes of employees constituting not less than 50 per cent of all employees in industrial workplaces employing 20 persons or more. The Workers' Representatives Convention, 1971 (No. 135), provides that, in granting the facilities which must be afforded to workers' representatives, account must be taken of the needs, size and capabilities of the undertaking. It is thus for the supervisory bodies to ensure that a reasonable criterion be applied, regarding in particular the size of the enterprise. The Termination of Employment Convention, 1982 (No. 158), permits measures to be taken by the competent authority or through the appropriate machinery, after consultation with the organizations of employers and workers concerned, to exclude from the application of the Convention or certain provisions thereof some limited categories of employed persons in respect of which special problems of a substantial nature arise in the light of, inter alia, the size of the undertaking that employs them. States parties making use of this option would be required under the terms of the Convention to indicate in their first report due under article 22 of the Constitution the categories thus excluded, giving the reasons for such exclusion, and to state in their

subsequent reports the position of their law and practice in respect to them, and the extent to which effect has been given or is proposed to be given to the Convention in respect of such categories.

### *Employment generation*

Small enterprises are also given special recognition by ILO instruments in relation to their potential contribution to employment generation. Thus the Preamble to the Employment Promotion and Protection against Unemployment Convention, 1988 (No. 168), mentions employment in SMEs among the forms of productive and freely chosen employment to be promoted.

However, it is primarily instruments concerning employment policy and human resources development which contain the most relevant provisions. In many of its comments on the application of the Employment Policy Convention, 1964 (No. 122), which is the basic Convention in this area and to date has received 83 ratifications, the Committee of Experts has drawn attention to the major role played by policies promoting small enterprises in pursuit of the objective of full, productive and freely chosen employment. In particular, the Committee has noted measures in favour of small enterprises that were contributing to countering unemployment in the context of structural adjustment or the transition to a market economy, and were assisting the integration of entrepreneurs and workers of the informal sector.

Part VI of the Employment Policy (Supplementary Provisions) Recommendation, 1984 (No. 169), which supplements the Employment Policy Convention (No. 122) and Recommendation (No. 122), 1964, is devoted to small enterprises. It recommends that account should be taken, in the framework of national employment policy, of the importance of small enterprises because of the employment possibilities that they offer, particularly for workers who have special difficulties. It recommends adopting, after consultation and in cooperation with employers' and workers' organizations, the measures necessary to promote complementary relationships between small enterprises and other enterprises, and to improve their working conditions as well as their access to markets, credit, technical expertise and advanced technology. The same Recommendation indicates that organizations of employers and workers concerned and enterprises should be encouraged to assist in the dissemination of general information on technological choices, in the promotion of technological linkages between large-scale and small-scale enterprises and in the setting up of relevant training programmes.

Thus, several standards recognize the importance of promotional measures to encourage employment creation in SMEs. However, it must be noted that they provide little guidance to constituents on how this is to be achieved.

### *Cooperatives*

The Cooperatives (Developing Countries) Recommendation, 1966 (No. 127), does not specifically mention SMEs, but nevertheless its relevance to the sector is implied and strong. This Recommendation details a large number of benefits to be accrued by small producers and individuals joining together, and sets out means by which cooperatives can be promoted. The standard is of clear value, but from the point of view of the needs of SME policy today, it offers only partial coverage.

### *Training*

Finally, as regards vocational training, the Human Resources Development Recommendation, 1975 (No. 150), draws attention to the advisability of specific directives concerning vocational training for branches of economic activity in which there are large numbers of small enterprises. It also emphasizes that, in branches of economic activity using obsolescent technologies and methods of work, advisory services should be organized for small entrepreneurs, and that information on possibilities of innovation in their work, and on related vocational training and other services which could be of assistance for this purpose, should be provided to them. It also indicates that, in these branches of activity, the needs of small entrepreneurs who ensure the initial vocational training of young persons should be taken into account.

In the same area, it is appropriate to refer to the Paid Educational Leave Convention, 1974 (No. 140), and Recommendation (No. 148), which are the only instruments to address the question of the financing of training. Convention No. 140 specifies that special provisions must be made where particular categories of workers, such as workers in small enterprises, find it difficult to fit into general arrangements, or where particular categories of undertakings, such as small undertakings, find it difficult to fit in with general arrangements, it being understood that the workers of these undertakings should not be excluded from the benefits of paid educational leave.

# CHAPTER VI

# ROLES FOR KEY STAKEHOLDERS

## 1. Government

### *Creation of a favourable economic climate*

Governments have primary responsibility for the provision of an enabling regulatory environment. As highlighted in Chapter III of this report, this covers monetary and fiscal regimes, trade and tariff policies, regulations relating to enterprise registration and land use, social standards including social security, and physical and informational infrastructures.

In a fast-changing global environment consultative machinery is necessary to review policies and regulations regularly, particularly as they relate to small-scale enterprises.

Governments should also promote an enabling social and cultural environment which places a high value on entrepreneurial attitudes and social standards.

Moreover, governments will need to facilitate the design and implementation of special programmes to assist disadvantaged groups.

### *High-level strategic coordination*

A further role of government is that of carrying out high-level strategic planning and coordination. Governments therefore have a role to play in national and regional planning in respect of setting up a broad policy and regulatory framework and coordinating policies and programmes. These would entail establishing or sponsoring the capacity-building institutions discussed in this report, including representative associations and workers' organizations.

As described earlier in the report, one means of furthering small and medium enterprise programmes is through high-level national "apex institutions to coordinate and support regional initiatives and harmonize small enterprise development programmes with those undertaken by various government ministries and agencies. Effective strategic coordination will require appropriate means of collecting and analysing data.

### *Decentralized public-private structures and partnerships*

The pace of change and the need to decentralize and focus on specific local conditions is leading to the questioning of established government practices. In general, and particularly in relation to small and medium-sized enterprises, centralized (often bureaucratic) structures are less effective than more flexible local organizations. New public-private initiatives are being developed in which

government agencies tend to stand back from policy implementation, thus encouraging private agencies, including employers' and workers' organizations, universities and other educational establishments, financial institutions, NGOs and specific interest groups, to take on more responsibilities.

Representatives of the private sector are being asked to participate on the boards of small and medium enterprise service institutions and, increasingly, on the boards of whole networks of interacting agencies, as in the case of the small enterprise region of Valencia in south-east Spain. In this way, services are becoming more relevant to the needs of clients and stronger networking synergies are being created.

### *Creator of consensus*

The uncertainties caused by rapid change, the need for a broad approach to the solution of pressing issues and sometimes the desire to pre-empt the possibility of conflict among potential rivals, have encouraged governments to adopt the role of "creator of consensus". Private bodies such as employers' and workers' organizations, which represent both large and small enterprises, as well as representatives of other associations and community groups, special interests, the educational sector and others, are now more than ever being encouraged to come together with local, regional and national governments to discuss development problems and propose initiatives.

There are many areas where initiatives can be taken to promote small enterprises: employment creation, environment, technology, credit, innovation, product diversification, exporting, training, and the identification of weaknesses in the economy.

A consensual approach has proved valuable where countries are relatively underdeveloped and there is a need for a rapid catching-up process; where countries are already advanced with relatively high living standards but there is a perceived need to improve productivity and innovation if standards are to be maintained; where old industry is in decline and there is a need for widespread restructuring and diversification; and where transition economies are experiencing acute dislocation of existing institutional, economic and social structures.

In Japan instruments for dealing with change at the national level are the consensus-forming Deliberation Councils. Each Council provides a forum for government officials and representatives from the private sector — business, labour, consumers, academics and the press — to discuss policy and market trends and generally to exchange information. Consensus within a Council is encouraged, and is apparently necessary if a policy is to stand a chance of success. In practice, the Councils are said to have real influence on policies.

At the regional level, an important factor in the success of one of the regions where small firms play a key role in the economy, Emilia Romagna in Italy, has been the role played by regional government in fostering a spirit of consensus among employers' and workers' organizations (see box 6.1). Recently, a tripartite committee has been formed to tackle problems facing small enterprises in the spheres of innovation, internationalization, financing, training and the environment.

In Latin America a policy of local level inter-institutional cooperation and consensus forming is currently being explored in several countries. The need to find solutions to urgent and crucial problems besetting local communities has given rise to

**Box 6.1. Italy: The EBER agreement**

In Italy an interesting initiative begun in 1993 has taken place in Emilia Romagna called the EBER agreement. In this agreement the three largest trade unions in the region and four of the main employers' associations representing artisan firms (those with less than 20 employees) have agreed on a number of "developmental" arrangements for small firms that have employees. Sixty per cent (48,000) of all artisan enterprises in Emilia Romagna with employees are covered. This agreement, funded by all parties, covers the retraining of workers, subsidies for the wages of firms going through temporary crises, funding for the promotion of industrial relations (including training employees to be trade union officers), funding for research into solutions to environmental and development problems, and funding for research and monitoring of economic trends in the small-firm sector.

The agreement has established a forum for future cooperative efforts to develop the small-firm sector by linking a whole range of issues related to social and economic development. By such means the competitiveness and levels of incomes and working conditions of small firms can be raised in a spirit of mutual complementarity.

Source: F. Pyke. *Comparing small and large firms in Europe: Prospects for incomes and working conditions*, June 1995.

ad hoc structures which bring together associations, local businesses, the municipal council, political parties and trade unions.

The ILO assists local authorities in a number of countries in Central and Eastern Europe in the design and implementation of consensus-based local economic initiatives which have a strong small and medium enterprise component. Examples are Molodechno in Belarus and Togliatti in Russia, where local socio-economic actors have arrived at a consensus on future development strategies.

## 2. Employers' and private sector organizations

In addition to their traditional role as partners in collective bargaining and negotiating on employment conditions, many employers' and other private sector organizations (including cooperatives) are expanding their activities, especially those of a developmental nature.

In most countries a majority of small enterprises are not members of representative organizations. In developing countries the membership levels are particularly low. This partly reflects entrepreneurs' lack of awareness of benefits and maybe their lack of time and resources to become involved, but also in some cases a slowness by existing employers' organizations to broaden their membership base. Employers' organizations can make an extra effort to attract small-scale entrepreneurs, possibly including the self-employed and those located in the informal sector.

The representation of entrepreneurs' interests vis-à-vis government has long figured high among the activities of employers' organizations. In some places, such as in certain regions of Italy, small-firm employers' organizations are strong and governments consult them closely. In many countries, however, small firms do not have strong representation, which goes against the interests of both small enterprises and government policy-makers, who may be denied valuable inputs to their deliberations. Employers' organizations may play an advocacy role towards government by voicing the concerns of small and medium-sized enterprises regarding policy and regulatory questions.

Low level of productivity and low awareness of quality concepts and tools are often serious constraints on SME growth and competitiveness. The tripartite National Productivity Board in Singapore, with the active support of the private sector, has run television shows with well-known music bands and other entertainment, skilfully integrated with information and case stories on quality-control circles, teamwork and similar productivity and quality-related tools. Such campaigns can play an important role in raising the general awareness of such concepts and facilitate their introduction into the workplace. Employers' organizations can become involved in such campaigns to raise quality, productivity and ethical standards.

Employers' organizations may, and in many cases already do, develop the capacity to provide direct support services to the SME sector in such areas as training, consultancy, access to credit, information, linkages with larger enterprises, marketing and export support and advising members on legal and social responsibilities.

There are many examples of employers' organizations that have extended their traditional roles to providing direct support services to their members. In India, the Mahratta Chamber of Commerce and Industry provides a range of services to small enterprises, including: consultancy services (for example, in respect of quality management and labour relations); information (in respect of, for example, rules and regulations pertaining to small enterprises); training; organizing exhibitions; and shared use of fax and other communication equipment (Sabade, 1993).

In Colombia, a dynamic leather industry association, ASOCUEROS, offers members a wide variety of courses, sponsors technical consultants and, in general, encourages networking and information sharing among firms (Levy, 1994). Around Guadalajara and León in Mexico, the small-firm footwear industry has been significantly assisted by entrepreneurial associations providing services like fiscal and labour consultancy, commercial assistance, managerial training and the organization of trade fairs (Rabellotti, 1994). Another example of service provision by representative organizations is given in box 6.2.

Employers' organizations may also become involved, along with workers' organizations, in the governance of decentralized public and public-private SME support institutions, including business start-up incubators, quality testing centres and training institutes.

The involvement of employers' organizations in such activities has increased strongly over recent years. In countries like Spain, Italy and Pakistan entrepreneurial associations in footwear, furniture, textiles, food and other sectors are involved on the boards of technical centres which provide the firms with services such as marketing, training, technological information, research and development and quality testing (Pyke, 1994).

**Box 6.2. Singapore: Employers' organizations organize their own service centre**

In 1989, with a grant from the Economic Development Board of Singapore, several chambers of commerce and industry associations organized the Enterprise Promotion Centre.

The Centre provides business information services, which take the form of regular circulars, guidebooks and directories on government assistance, business services and business solutions. Consultancy services are available for developing quality management systems, the formulation of business plans, the setting up of financial and management accounting systems, industrial engineering and human resource management. Talks and seminars are organized regularly to help entrepreneurs upgrade their managerial capabilities.

The Enterprise Promotion Centre has also set up an electronic network, EPC-Net, to provide the business community with an efficient channel for communication, information dissemination and exchange of documents. EPC-Net offers electronic mail services, electronic bulletin board, on-line information services, electronic data interchange services and international links.

As a private sector organization enjoying government support, the Enterprise Promotion Centre has become an effective catalyst for enterprise promotion.

Source: G. Abraham: "One stop service for GSEs: The Enterprise Promotion Centre", in C. A. Balasuriya, A. P. Capriati and H. G. Waesch (eds.): *New and innovative concepts for small-scale enterprise promotion* (Ho Chi Minh City, 1992).

Employers' organizations can be important vehicles for rapid dissemination of information on best practices. This can be done through publications or through specially convened experience-exchange groups and training sessions. The existence of associations which bring entrepreneurs into contact with one another can provide significant advantages for launching further cooperative projects (see earlier references to credit associations and other organizations, such as those in Benin, that have progressed to a range of collaborative activities). Employers' organizations may thus act as vehicles for collaborative action and mutual learning processes among small and medium-sized enterprises.

Employers' organizations may also participate with workers' organizations and other interest groups in councils, task forces and other bodies at the central and local level established to deal with important economic and social issues, including policies and programmes affecting the SME sector.

South Limburg in the Netherlands is an example of a declining heavy industry that underwent extensive restructuring. During the 1960s and 1970s all of its 12 coal-mines were closed, causing high unemployment and a shortage of employment opportunities. In a concerted effort involving the national Government, the provincial Government of Limburg, the municipalities and the employers' and workers' organizations, a reorganization plan was produced. Today, the economic structure, previously entirely dependent on mining, is much more diversified and resilient.

### 3. Workers' organizations

Like employers' organizations, workers' organizations may add new activities, especially of a developmental kind, to their traditional bargaining role.

Representation in workers' organizations is relatively low in the SME sector, especially in developing countries. This partly reflects a lack of resources. Attempts to broaden membership are however increasing, with some organizations considering catering for workers in the informal sector. In the Philippines the Trade Union Congress of the Philippines (TUCP) amended its constitution and by-laws in 1990 to institutionalize formally membership of people in the informal sector. The TUCP has created a Filipino Workers' Development Fund to assist members in the informal sector, among other social groups, and has contributed funds to credit unions that are serving the informal sector (ILO, 1995b). The Trades Union Congress of Ghana has included the informal sector in the scope of its organization. Several sectoral associations of the self-employed have been formed, and their services include pooling resources and providing credit to members, seeking legal protection for informal sector businesses, and safeguarding the market interests of the self-employed businesses.

Workers' organizations can make an extra effort to attract workers in small-scale enterprises as well as the self-employed and those located in the informal sector.

For example, the Organization of Tanzania Trade Unions (OTTU) is in the process of launching its own trades union for the informal sector. This follows previous studies, seminars and exchange visits between Ghana's TUC and OTTU which have shown the venture to be viable. The ILO's interdepartmental project on the informal sector has been providing technical support for the establishment of this unit. Similarly, in Colombia the main trade unions, the Single Confederation of Workers (CUT), the Confederation of Workers of Colombia (CTC) and the General Confederation of Democratic Workers (CGTD), have established special departments to organize workers from the informal sector and to institutionalize their membership of the union.

Workers' organizations may participate with employers' organizations and other interest groups in councils, task forces and other bodies established at the central and local level to deal with important economic and social issues, including policies and programmes affecting the SME sector.

Such bodies would include the national, regional and local tripartite committees discussed in this report, including those dealing with active labour market policies, and also bipartite worker-employer councils.

Workers' organizations may also explore ways to promote socially and economically progressive restructuring while maintaining appropriate social safety nets, and of supporting retraining and the pursuit of employment and self-employment in the SME sector (see box 6.3).

Workers' organizations may also become involved in the development and implementation of various employment and income-generation schemes, such as workers' cooperatives and worker-owned enterprises.

In Italy the General Confederation of Labour (CGIL) has established the Società Multiserva Impresa e Lavoro (SMILE), a non-profit organization that aims to promote and support new enterprises, especially (but not only) cooperatives, and especially (but not only) in the south of the country. SMILE provides technical assistance

**Box 6.3. Germany: A tripartite approach to restructuring**

In the German Land of North Rhine-Westphalia programmes of regional strategic planning were launched in the late 1980s to convert the regional economy from its heavy dependence on coal and steel to a more modern mixed and diversified economy. Under the chairmanship of the regional government, various groups (including employers and trade union organizations, local government, chambers of commerce and industry, the public labour administration and the universities) met in local development conferences to search for a consensus on a number of projects geared towards:

- improving local technology and innovation and the quality of the labour force;
- creating new employment;
- modernizing the local infrastructure; and
- improving the environment and energy base.

Source: W. Sengenberger, G. W. Loveman and M. J. Piore (eds.): *The re-emergence of small enterprises: Industrial restructuring in industrialized countries* (Geneva, International Institute for Labour Studies, 1990).

(especially support for new start-up enterprises), training (especially upgrading of skills) and information services and promotes linkages between enterprises, and between enterprises and institutions, that can result in new production initiatives.

In the United Kingdom the Wales Trade Union Council has established the Wales Cooperative Development Centre to create employment through cooperative enterprises, to provide business advice to small and medium-sized enterprises and to carry out training. One cooperative which the Cooperative Development Centre has helped to establish is the Cynon Valley Clothing Company, a women's cooperative employing (and collectively managed by) 30 women who successfully went into business in 1989 after a private company previously employing them closed down (ENSR, 1994).

In South Africa the National Council of Trade Unions (NACTU) has formed an investment corporation called NACTU Holdings Limited with an investment portfolio of R.70 million. It will operate as a profit-making business venture and its proceeds will bolster NACTU's financial base.

Workers' organizations may also increase their involvement on the boards of small and medium enterprise service institutions, such as business start-up agencies and training institutes and through these institutions, or otherwise, become involved in the promotion of training initiatives and experience exchange groups between workers, and between workers and entrepreneurs.

In Greece the Metalworkers Trade Union of Northern Greece provides seminars to teach metalworking professional qualifications to technicians in small and medium-sized enterprises. The seminars are offered in cooperation with the Department of Mechanical Engineering of the Technical University of Thessaloniki.

In Denmark, the Regional Trade Union of Commercial and Clerical Employees has joined with the Danish Employers' Confederation and the Aarhus School of Commerce to train the unemployed in learning specialist skills in exporting, while a

consortium of trade unions, employers' organizations and local authorities are working to create export-oriented jobs specifically in small firms and are exchanging information with and collaborating with similar consortia in other European countries (ENSR, 1994).

Workers can become involved with employers' organizations in campaigning for improvement of conditions conducive to ensuring quality and productivity, including better working practices and high ethical standards.

### 4. The role of international organizations and other bodies

In addition to the social partners whose possible roles in generating employment through efficient and competitive SMEs have already been covered in the first three sections of this chapter, there are other organizations which can play important facilitating roles. International organizations can contribute to the systematic exchange of best practice in terms of policies and programme approaches for generating employment through support to the SME sector.

Similarly there is a need to facilitate and maintain linkages between national and international institutions (including workers' and employers' organizations) involved in SME promotion to facilitate exchange in such areas as staff and ideas, training materials, training methodologies and other resource materials, and research findings and other data on SMEs. This can be supported by international meetings and discussion groups on approaches to employment generation through SME promotion.

Another important area is the creation of linkages and partnerships between SME support agencies and representative organizations to facilitate international SME partnerships, alliances, subcontracting arrangements and other commercial linkages. Such arrangements could be further supported by promoting access by SMEs to national and international databases in such areas as market information, regulations, technology and product standards.

The ILO, with its unique tripartite structure could further expand a number of its current activities aimed at tapping the full employment-generation potential of the SME sector.

Another area is the provision of advisory services to governments in the formulation of policy and regulatory measures to support a growing and dynamic small enterprise sector, while ensuring that basic social concerns are covered in such areas as occupational safety and health, working conditions, social security and other aspects promoted by international labour standards.

The ILO may also:

- support capacity building among employers', workers' and other concerned organizations so that they play an effective role in the support and promotion of SMEs, for example by strengthening their ability to participate in national participative planning processes and by helping them to assist retrenched persons taking up employment and self-employment in SMEs;
- support cooperative organizations to enable them to improve the productivity and efficiency of their member societies;
- carry out comparative international research on effective strategies to promote productive, sustainable employment creation through SMEs; such applied

research can provide important support to the social partners in their search for practical ways to translate policies into cost-effective employment programmes centred around productive and competitive SMEs;

— support, through technical assistance programmes and advisory services, the building of local capacity, and plan and implement cost-effective programmes to support SMEs in such areas as training, consultancy, credit, and access to information and markets;

— foster, where possible and applicable, a tripartite approach to SME development policies and programmes, including the monitoring of compliance with social and labour market regulations and standards in such areas as working conditions, child labour, social security;

— study and explore further the role of SME programmes in alleviating the problems facing countries emerging from armed conflict and other calamities, as well as the problems faced by disadvantaged groups such as the disabled, indigenous and tribal peoples, and unemployed youth.

## QUESTIONNAIRE

In accordance with article 39 of the Standing Orders of the International Labour Conference, governments are requested to consult the most representative organizations of employers and workers before finalizing their replies to the following questionnaire, and to send their replies, indicating the reasons for each reply, so as to reach the International Labour Office in Geneva by 1 June 1996 at the latest.

### I. Form of instrument

*1. Do you consider that the International Labour Conference should adopt an international instrument concerning the general conditions to stimulate job creation in small and medium-sized enterprises (SMEs)?*

*2. If so, do you consider that the instrument should take the form of a Recommendation?*

### II. Preamble

*3. Should the instrument include a preamble which would make reference to a number of related existing instruments, such as:*

*(a) the Employment Policy Convention, 1964 (No. 122), and the Employment Policy (Supplementary Provisions) Recommendation, 1984 (No. 169)?*

*(b) the Human Resources Development Convention, 1975 (No. 142), and the accompanying Recommendation (No. 150)?*

*(c) the Cooperatives (Developing Countries) Recommendation, 1966 (No. 127)?*

*(d) others? (If so please specify.)*

### III. Purpose, scope and definition

*4. Should the instrument recognize that SMEs have a fundamental role to play in:*

*(a) the promotion of full, productive and freely chosen employment?*

*(b) greater access to income-earning opportunities?*

*(c) economic growth and the ability to react flexibly to changes?*

*(d) increased domestic savings and investments?*

*(e) other areas? (Please elaborate.)*

*5. Should the instrument address:*

*(a) the policy and legal framework as well as the support structures, programmes and other initiatives which can facilitate the development and growth of SMEs?*

*(b) quantitative as well as the qualitative aspects (terms and conditions of employment, working conditions, social protection, etc.) of employment in SMEs?*

*6. Should the instrument apply to:*

*(a) SMEs in all economic sectors (i.e. industrial, service and extraction) except farming?*

*(b) all types and forms of ownership (i.e. private and public companies, cooperatives, partnerships, family enterprises, sole proprietorships and others)?*

*(c) both formal and informal sector activities?*

*7. (1) Should the instrument recognize that the definition of an SME varies from country to country and that the detailed definition of an SME should be determined by each Member in line with local conditions?*

*(2) Should the instrument none the less define an SME as an enterprise employing from one to 100 persons? If not, please suggest another suitable definition.*

## IV. Policy and legal framework

*8. Should the instrument emphasize the importance of stability of:*

*(a) the economic environment (i.e. rates of inflation, interest, exchange and tax) through appropriate fiscal and monetary policies?*

*(b) rules governing subjects such as property rights, zoning and enforcement of contracts?*

*9. Should the instrument provide for policies to promote efficient and competitive SMEs which are able to provide productive and sustainable employment opportunities under adequate social conditions? If so:*

*(1) Should such policies include the objective of creating an environment which provides equal opportunity for all sizes and types of enterprises in such areas as access to credit, foreign exchange, imported inputs and taxation?*

*(2) Should such policies also address commonly perceived constraints to the development and growth of SMEs, such as:*

*(a) insufficient access to credit?*

*(b) low levels of technical and managerial skill?*

*(c) inadequate information?*

*(d) low levels of productivity and quality?*

*(e) insufficient access to markets?*

*(f) inappropriate, inadequate or overly burdensome requirements applicable to SMEs as regards, for instance, registration, licencing and reporting?*

*(g) others? (Please specify.)*

*(3) Should the instrument encourage the adoption of specific policies aimed at upgrading the informal sector to become part of the organized sector?*

*10. Should such policies be formulated with due consideration to and in full coordination with other policies in such areas as fiscal and monetary matters, trade and industry, employment, labour, social protection and occupational safety and health? Comments:*

*11. When formulating the policies referred to in question 9 above should the government consult:*

*(a) the social partners?*

*(b) other concerned parties such as non-governmental organizations, small enterprise development institutions and academic bodies?*

*12. Should the instrument encourage governments to:*

*(a) undertake a major review of the impact of existing policies and regulations on SMEs?*

*(b) undertake a review, in consultation with the social partners, of labour regulations to determine whether they meet the special needs of SMEs and their workers?*

*(c) undertake a review of the existing mechanisms for social protection to determine whether they meet the needs of SMEs and their workers, and, where appropriate, consider a range of supplementary measures such as voluntary schemes, cooperative initiatives and others?*

*(d) establish mechanisms to review and update, on a regular basis, existing and proposed policies?*

*13. Should the instrument provide for governments to improve the collection of adequate national data on the SME sector as an input to the policy-making and implementation process?*

*14. Should the following, where appropriate, be decentralized to the regional and local level:*

*(a) formulation of SME policies and regulations?*

*(b) administration of SME policies and regulations?*

## V. Development of an enterprise culture

*15. Should the instrument provide that measures should be taken to create and strengthen an enterprise culture which emphasizes individual initiative and enterprise creation, productivity, quality, fairness and adequate social standards? If so, should they be pursued through:*

*(a) introducing entrepreneurial and related skills development into the system of education and training?*

*(b) designing and implementing mass media awareness campaigns to promote:*

*(i) lawful and socially desirable business practices?*

*(ii) higher standards in areas such as productivity and working conditions?*

*(iii) higher consumer expectations as regards standards of design and quality?*

*(iv) entrepreneurial role models and award schemes for both men and women?*

*(c) other means? (Please specify.)*

## VI. Development of an effective SME service infrastructure

*16. Should the instrument provide that the competitiveness, growth and job creation potential of SMEs may be enhanced through the provision of a range of direct support services? If so, should these include:*

*(a) managerial training and skills enhancement?*

*(b) research and consultancy services?*

*(c) access to credit?*

*(d) quality testing and measurement?*

*(e) marketing assistance?*

*(f) packaging services?*

*(g) product design?*

*(h) business start-up assistance?*

*(i) information services?*

*(j) export promotion?*

*(k) advice regarding technology?*

*(l) physical infrastructures such as water, electricity and premises?*

*(m) support for innovation?*

*(n) legal, accounting and other professional services?*

*(o) other support services? (Please specify.)*

*17. Should the instrument provide that, as far as possible, the delivery of such services should ensure the highest degree of relevance and efficiency through such means as:*

*(a) adapting the specific services and their delivery to the particular prevailing economic, social and cultural conditions?*

*(b) encouraging private sector involvement in the delivery of services through, for example, trade associations, workers' organizations, semi-public organizations and private consultants?*

*(c) decentralizing the delivery of services, thereby bringing them as physically close to the SMEs as possible?*

*(d) ensuring strong involvement of SMEs in the determination of services to be offered?*

*(e) providing services tailored to the specific needs of SMEs in different sectors and of different sizes?*

*(f) promoting easy access to an integrated range of services through "single window" arrangements and referral services?*

*(g) aiming towards self-sustainability through a reasonable degree of cost recovery from SMEs and other sources?*

*(h) ensuring professionalism and accountability in the management of service delivery?*

*(i) establishing mechanisms for continuous monitoring, evaluation and updating of services?*

*(j) other means? (Please specify.)*

*18. Should the instrument provide that, whenever possible, services should be designed in such a way as to include productivity-enhancing approaches which promote efficiency and satisfactory labour practices and working conditions?*

*19. Should the instrument promote improved access by SMEs to finance and credit? If so:*

*(1) except in the case of particularly vulnerable groups of entrepreneurs, should credit and other financial services be provided as far as possible on commercial terms to ensure their sustainability?*

*(2) should supplementary measures be considered to overcome such problems as complicated procedures, inadequate collateral from SMEs and high transaction costs, by means of, for example, non-governmental financial retail agents and poverty-oriented development finance institutions?*

*(3) should SMEs be encouraged to organize in mutual guarantee associations?*

*20. Should the instrument encourage linkages between large and small enterprises? If so, should measures be taken to safeguard and promote the legitimate interests of SMEs in subcontracting?*

*21. Should the instrument promote linkages between SMEs themselves to encourage mutual learning as well as resource and risk sharing? If so, should there be specific encouragement of service cooperatives and similar structures?*

*22. Should the instrument provide that special measures should be taken to address the needs of the following categories of entrepreneurs:*

*(a) aspiring entrepreneurs affected by structural adjustment?*

*(b) women?*

*(c) demilitarized personnel?*

*(d) disabled persons?*

*(e) other categories? (Please specify.)*

## VII. Roles of the government and employers' and workers' organizations

*23. Should the instrument encourage governments, while standing back from direct involvement in policy implementation, to focus their efforts mainly on:*

*(a) establishment of broad policy and legal frameworks?*

*(b) development of national and regional strategies?*

*(c) coordination of policies and programmes to support SMEs?*

*(d) provision of broad-based infrastructure in such areas as energy, telecommunications and transport?*

*(e) other areas? (Please specify.)*

*24. Should the instrument provide that part of the government's role is the establishment and sponsoring of organizations, other than employers' and workers' organizations, which:*

*(a) effectively support the growth and competitiveness of SMEs?*

*(b) promote observance of international labour standards in SMEs in such areas as social protection and the elimination of child labour?*

*25. Should the instrument provide that governments should consider the establishment of an apex SME institution which would generally coordinate and support the initiatives related to SME promotion?*

*26. Should the instrument encourage the following types of involvement of employers' organizations in SME development:*

*(a) voicing the concerns of SMEs towards government regarding the policy and legal frameworks in which they operate?*

*(b) provision of direct support services such as training, consultancy, facilitating access to credit, marketing support, promoting linkages with larger enterprises and similar services?*

*(c) involvement in the governance of national, regional and local SME-oriented institutions which provide support in such areas as training, consultancy, business start-up and quality?*

*(d) participation in councils, task forces and other bodies at central, regional and local levels established to deal with important economic and social issues, including policies and programmes affecting SMEs?*

*(e) taking part in the development of economically and socially progressive restructuring (by means of, for example, retraining and promotion of self-employment) while maintaining appropriate social safety nets?*

*(f) becoming involved in promotion of exchanges of experience and establishment of commercial linkages between SMEs?*

*(g) participating in the monitoring of social and labour market issues regarding SMEs, including terms and conditions of employment and working conditions?*

*(h) becoming involved in campaigns to raise quality, productivity and ethical standards and to achieve gender equality?*

*(i) others types of involvement? (Please specify.)*

*27. Should the instrument:*

*(a) encourage the establishment of independent representative organizations of SMEs?*

*(b) alternatively, encourage more broadly based employers' organizations to extend their coverage of SMEs? If so, should it encourage them to establish special SME departments?*

*(c) encourage the establishment of independent representative employers' organizations for the self-employed?*

*(d) alternatively, encourage more broadly based employers' organizations to establish special sections for the self-employed?*

*28. Should the instrument encourage the following involvement of workers' organizations in SME development:*

*(a) voicing the concerns of workers in SMEs towards government regarding the policy and legal frameworks in which SMEs operate?*

*(b) provision of direct support services such as training, consultancy, facilitating access to credit, marketing support, promoting linkages with larger enterprises and similar services?*

*(c) involvement in the governance of national, regional and local SME-oriented institutions which provide support in such areas as training, consultancy, business start-up and quality?*

*(d) participation in councils, task forces and other bodies at central, regional and local levels established to deal with important economic and social issues, including policies and programmes affecting SMEs?*

*(e) taking part in the development of economically and socially progressive restructuring (by means of, for example, retraining and promotion of self-employment) while maintaining appropriate social safety nets?*

*(f) becoming involved in promotion of exchanges of experience and establishment of commercial linkages between SMEs?*

*(g) participating in the monitoring of social and labour market issues regarding SMEs, including terms and conditions of employment and working conditions?*

*(h) becoming involved in campaigns to raise quality, productivity and ethical standards and to achieve gender equality?*

*(i) other types of involvement? (Please specify.)*

*29. Should the instrument:*

*(a) encourage the establishment of independent representative organizations of workers in SMEs?*

*(b) alternatively, encourage more broadly based workers' organizations to extend their coverage of workers in SMEs? If so, should it encourage them to establish special SME departments?*

*(c) encourage the establishment of independent representative workers' organizations for the self-employed?*

*(d) alternatively, should it encourage more broadly based workers' organizations to establish special sections for the self-employed?*

## VIII. International collaboration

*30. Should the instrument recommend international collaboration in the following areas:*

*(a) systematic exchange of information on best practices in terms of policies and programmes to create jobs in SMEs?*

*(b) creation of linkages between national and international bodies and institutions that are involved in SME development, including employers' and workers' organizations, in order to facilitate:*

(i) *exchange of staff and ideas?*

(ii) *exchange of training materials, training methodologies and reference materials?*

(iii) *compilation of research findings and other data on SMEs and their development?*

(iv) *establishment of international SME partnerships, alliances, subcontracting arrangements and other commercial linkages?*

(v) *other types of linkages? (Please elaborate.)*

(c) *international meetings and discussion groups on approaches to job creation through SME development?*

(d) *systematic research into the structure, effectiveness and key success factors for SME promotion in a variety of contexts and countries?*

(e) *promotion of access by SMEs to national and international databases in such areas as market information, laws and regulations, technology and product standards?*

*31. Should the instrument encourage Members to adopt positions that are in accordance with the purposes of the proposed instrument when they participate in decision-making in other international organizations?*

*32. Any other overall comments which you would like to add?*

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ANNEX

## RESOLUTION CONCERNING THE PROMOTION OF SMALL AND MEDIUM-SIZED ENTERPRISES

*(Adopted on 23 June 1986)*

The General Conference of the International Labour Organization,

Noting the report on the Promotion of Small and Medium-Sized Enterprises submitted at its 72nd Session (1986),

Having discussed national and international experience and development with regard to small and medium-sized enterprises that has taken place since the adoption by the International Conference of:

— a resolution concerning the contribution of small and medium undertakings to economic and social progress and to the creation of employment, in particular in developing countries, at its 60th Session (1975),

— a further resolution concerning the training and retraining of managers in both private and public undertakings as well as the encouragement of the spirit of entrepreneurship especially in developing countries at its 67th Session (1981),

— the Conclusions concerning the ILO's future activities with regard to the social aspects of industrialization at its 69th Session (1983), and

— the provisions concerning small enterprises contained in the Employment Policy (Supplementary Provisions) Recommendation (No. 169) at its 70th Session (1984),

Having examined the ILO's activities in the field since 1975;

1. Recognizes that governments, employers, workers and their respective organizations have interests and responsibilities in the area of small and medium-sized enterprises.

2. Appeals to member States to give effect to the part relating to national and international action in the Conclusions concerning the promotion of small and medium-sized enterprises adopted by the International Labour Conference at its 72nd Session (1986).

3. Invites the Governing Body of the International Labour Office to request the Director-General to give due consideration to these Conclusions in ILO action and activities.

### Conclusions concerning the promotion of small and medium-sized enterprises

#### I. Introduction

1. A universally accepted definition of small and medium-sized enterprises (SMEs) does not exist. It is more appropriate for each country to develop its own definition according to national, social and economic conditions. With this qualification in mind, the following conclusions are relevant to various types of SMEs irrespective of management or type of ownership.

2. SMEs can play a significant role by marshalling entrepreneurial initiative into the economic and social development of all countries side by side with large-scale enterprises with which they should enjoy a balanced interdependence.

3. SMEs are one of the vehicles for social progress, for employment creation, for stimulating investment at lower cost, for performing complementary activities to those

performed by large firms and for supporting policies of regional and local decentralization of economic activities. Furthermore, they can stimulate the development of a pool of managers, entrepreneurs and skilled workers.

4. Because of the above factors many governments have adopted policies, including tripartite policies, established institutions and set up programmes to promote SMEs. These initiatives vary from one country to another. Furthermore, the pace of progress in these countries has been uneven.

5. In their various initiatives governments should fully involve employers and workers and their respective representative organizations. This tripartite approach applies to all the conclusions which follow.

## II. National and international action

6. When deciding actions directed towards the promotion of SMEs account should, as appropriate, be taken of national circumstances.

### *Role of governments*

7. Governments should —

(i) in national development policies and plans, define explicitly and recognize the social and economic contributions of the SME sector and the actions to be taken to enable SMEs to make these contributions;

(ii) make one of their primary objectives the creation and maintenance of a social and economic climate conducive to the enhanced rate of creation and healthy development of SMEs with particular attention to employment creation and other economic goals and measures such as stable currencies, low rates of inflation, removal of barriers to trade, availability of finance at appropriate interest rates and equitable levels of taxation;

(iii) review the regulations and administrative procedures of the various departments and agencies governing the creation and operation of all forms of enterprises with a view to simplifying and streamlining those regulations and procedures where compliance imposes a disproportionately heavy burden upon SMEs, while at the same time fully protecting workers' rights;

(iv) in the design and execution of programmes of promotion of SMEs, bear in mind the heterogeneity of SMEs in respect of size, type of activity, geographical location, etc., which requires different approaches for different sectors and target groups;

(v) in addition, build a climate conducive to growth, providing incentives to enhance the creation, survival and growth of SMEs. Such measures could be for fixed or extended periods in accordance with national conditions and experience;

(vi) where appropriate, be prepared to facilitate the execution of SME promotion programmes by other organizations including organizations of employers and workers and NGOs, and to evaluate the success of such programmes;

(vii) design and execute programmes of promotion of SMEs, as far as possible on a decentralized basis, in conjunction with individual local and regional programmes, using the "one-window" format whereby all the components of an assistance package are available from or through a single institution, where appropriate;

(viii) devise, if necessary, appropriate legal provisions for the establishment of SMEs taking into account the size of the enterprise, enterpreneurial risks, and the possibilities of cooperation between enterprises;

(ix) establish and promote the production of statistics specifically identifying SMEs, without placing an undue burden on the enterprises concerned.

*Role of trade associations*

8.

(i) Associations should intensify their actions in respect of SMEs both in promoting the interests of SME members and in enhancing the effectiveness of government programmes of assistance to SMEs; they should provide training and advice on managerial and financial aspects and on labour relations, working conditions and international labour standards;

(ii) very small enterprises, cottage industries, artisans, craftworkers, etc., should be encouraged to organize themselves voluntarily on a trade or cooperative basis which could be affiliated with other associations of their choice.

*Other NGOs*

9. NGGs should participate actively in SME promotion programmes, particularly those aimed at special target groups and sectors (e.g. urban informal sector and rural areas, women and youth) in which the special characteristics of NGOs make them extremely valuable collaborators.

*Developmental activities*

10. National SME development strategies and programmes should differentiate between the promotion of existing and the creation of new enterprises. In both cases, approaches need to be comprehensive in that they should comprise a combination of several types of assistance, such as credit, management training, counselling, extension services, entrepreneurship development, industrial estates, workshop clusters, common facilities, ancillary equipment, raw materials procurement, promotion, where appropriate, of legitimate subcontracting or franchising, technological information services, product design and development, trade or export promotion, etc.

*Management training and entrepreneurial development*

11.

(i) SMEs, particularly in developing countries, need to reinforce management training for various types and sizes of SMEs. Training should be given at a wide variety of institutions, including educational institutions and professional organizations. The principal types of training needed include technical and vocational training of managers and workers, and management training of managers and owners. Regarding training methods, there is a great need to actively develop practical forms of group training and effective learner-based self-development methods through continuing education programmes;

(ii) in management training, special emphasis should be placed on business planning, organization of work, loan negotiations, purchasing and inventory management, marketing, financial control, personnel management and occupational safety and health;

(iii) there is an acute need for entrepreneurship development courses to improve latent entrepreneurial talent. Entrepreneurship development should be open to both men and women on an equal basis and should be diversified for special categories such as youth,

refugees, redundant civil servants and public and private sector employees, jobless persons, migrants and handicapped persons;

(iv) vocational training in many countries needs to be associated with complementary programmes combining it with management and entrepreneurial training which could stimulate the trainees' interests in creating small enterprises or becoming self-employed;

(v) where a need exists, it is necessary to expand the pool of trainers and other professionals and consultants such as accountants, solicitors, industrial relations specialists, business administrators, industrial engineers and teachers specialized in assisting SMEs;

(vi) in order to encourage better practices in SMEs and better curricula in educational and training institutions there is need to promote collaboration between them.

*Extension services*

12. There is a need to reinforce and decentralize extension services and study ways of making these services more effective.

*Technology*

13.

(i) SMEs are an important source for the development of new technologies, particularly in industrialized countries. The need exists for the adaptation of technology to local and SME needs, especially in developing countries, for appropriate research and for the dissemination of information on appropriate technology and the training of managers and workers in its application. The transfer of obsolete technology which is hazardous should be prohibited;

(ii) the establishment of technology centres that provide assistance in technology choice and the use of mass media particularly in disseminating information on technology to rural areas as well as the use of extension agents trained in specific technologies should be supported. Increased industrial and technological cooperation between developing countries and between them and a developed country in transferring and adapting technology to SMEs also deserves strong support. Furthermore, developing countries will need to redirect their existing research and development efforts specifically to promote introduction of new technologies, taking into account social and economic priorities and impacts;

(iii) universities and technical colleges should be given a greater role in the development and dissemination of technologies in conjunction with SMEs.

*Marketing*

14.

(i) The development, encouragement and expansion of internal and external markets is a major preoccupation for SMEs. Some SMEs feel they do not have the opportunity to compete freely and to have access to distribution channels and some suffer from unfair competition. Marketing assistance could be effectively developed by promoting linkages *between enterprises of various sizes, by way of legitimate subcontracting, where* appropriate, franchising or other forms of inter-firm cooperation;

(ii) some governments allocate preferentially a range of sectoral activities for SMEs. This can, under certain circumstances, be workable, provided this privileged treatment is limited in scope and time. Public procurement from SMEs should be encouraged;

(iii) organizing SMEs for export marketing should be encouraged through coordinated efforts, assisting in quality standards, and in providing information on foreign markets as well as by assisting them in representation overseas.

*Finance*

15.

(i) To help strengthen the financial position of SMEs it is necessary to have a good network of financial institutions and programmes to facilitate the flow of capital to them at appropriate rates of interest;

(ii) governments should also seek by various means to encourage entrepreneurs to use their own funds;

(iii) whereas in some industrialized countries institutions such as development banks and commercial banks are paying more attention to the needs of SMEs, in most countries and to a greater extent in developing countries, every effort must be made to encourage banks and development corporations to assist SMEs. In this connection the establishment of schemes such as guarantee funds and programmes can be helpful;

(iv) capital is particularly tight for newly established entrepreneurs and for rural producers and craftworkers. In this respect, governments should establish specific trust funds. The use of non-traditional sources of financing such as cooperatives, associations or solidarity organizations can be helpful;

(v) in many countries, there is a need to liberalize or ease the terms of loans and to simplify the procedure and expedite the granting of loans to SMEs. Equally, the training of bank personnel in appraising and supervising small loans needs to be intensified;

(vi) initiatives aimed at the establishment of sound venture capital concerns and joint ventures need to be supported.

*Labour and social aspects*

16.

(i) The promotion of SMEs should be accompanied by sound policy to protect the legitimate interests of workers in this sector, including recognition of the important role of their organizations;

(ii) such a policy should strive at improving and ensuring the safety and health as well as satisfactory working conditions for those employed in SMEs;

(iii) compliance with international labour standards should be adhered to;

(iv) those standards dealing with child labour and freedom of association have been highlighted for particular attention;

(v) recognizing the need to promote the establishment and maintenance of tripartite consultative machinery at national level to deal with industrial relations, there is equally a need to disseminate information about good personnel policies in SMEs and to train managers and workers as well as labour administrators in sound industrial relations relevant to this sector;

(vi) similarly, a need exists for reviewing industrial legislation and directives so as to streamline and simplify administrative procedures, while fully protecting workers' rights;

(vii) attention should be given to the status of small entrepreneurs in national social security systems.

17. In developing policies relating to SMEs, governments should give clear recognition to the requirement that the prospect of legitimate profits, which should be equitably distributed, is essential to the establishment and maintenance of any business.

*Sectoral and target group activities*

18. In the interests of enhancing the effectiveness of SME promotion programmes, consideration should be paid to the use of sector-specific and target group-oriented programmes.

*Rural development*

19.

(i) For developing countries in particular, the promotion of small enterprises in rural areas should command a high priority. Effective training programmes backed up by extension services and assistance in credit need to be developed at the grass-roots level;

(ii) NGOs in particular play a very useful role in this respect and their efforts need to be supported.

*Informal sector*

20. In view of their importance for employment creation, in particular in developing countries, small enterprises in the informal sector can require intensified action by governments and non-governmental organizations with the aim of integrating them into the national economy. This approach could involve assistance substantially different from assistance to small enterprises in general and require special delivery channels, able to take into account the characteristically low levels of schooling, skills, capital and know-how, and be capable of adopting participative, informal approaches.

*Youth*

21. Every effort should be made to promote the employment of youth. Within this context, initiatives to inject elementary management and entrepreneurial training in vocational, technical and normal education deserve to be supported. Such efforts could stimulate self-employment and introduce an awareness of the potential that exists for creating SMEs.

*Women*

22. Women constitute an important part of the working population, especially in SMEs. However, many still suffer from social and economic discrimination in employment, education and training, working conditions and access to income-earning possibilities. Positive action must be taken at the national and international levels to ensure equal opportunities in employment, training, finance and access to all facilities aimed at promoting SMEs. Every effort should be made to promote the equal access of women to general SME development programmes. The impact of such programmes on the situation of women should be continuously monitored.

*The disabled*

23. Promising possibilities exist for the disabled to be associated with the creation or operation of certain types of SMEs either in sheltered or in open employment depending on the disability. Efforts should be made to encourage initiatives taken in this direction.

## III. Future action by the ILO

24. The contribution made by the ILO to the development of SMEs and entrepreneurship has been considerable. In addition to promoting new ideas and sensitizing member States to the potential of the sector and to its various problems, the ILO has provided specific assistance to member States in a number of cases. However, the importance of the sector to employment generation and the fact that entrepreneurial initiative and SME development continue to face serious difficulties in many countries, call for an expansion and intensification of the ILO's efforts in SME promotion within the limits of the ILO's mandate. These efforts should be coordinated with the programmes of other national and international organizations.

25. The establishment of an Office-wide action programme in this area should be pursued. SME promotion and entrepreneurship development should play a major role in the ILO's activities in employment development, in the rural and informal sectors as well as in programmes for youth and women and those priority sectors where economic and social development is particularly difficult. Small enterprise and entrepreneurship development should be treated as an area of special emphasis in the ILO mid-term plans and biennial programmes and budgets. In this connection, the ILO should allocate more financial resources and personnel to its activities directly related to the assistance of SMEs, as much as possible by shifting resources from other programmes more remote from direct application. Increased attention ought to be paid to labour and social aspects of SME development.

26. While fully respecting the specific social and economic conditions under which SMEs develop in every member State, ILO programmes should focus on identifying common trends and problems and enhancing exchange of experience among countries. The tripartite approach should be consistently applied to all ILO programmes aimed at SME promotion. Member States should be encouraged to develop tripartite machinery for establishing and monitoring SME development policies and programmes.

### *Promotion of SMEs*

*Government involvement*

27.

(i) The ILO should continue to study ways and means whereby governments promote and assist SMEs and provide advice in specific instances at governments' request. Comparative studies of government policies, programmes and institutional arrangements should be published. Training of policy-makers concerned with SME promotion should be expanded with the participation of the Turin Centre and the regional centres;

(ii) technical assistance in specific developmental activities such as training or finance should be based on a thorough study of the policy environment for SME development and of specific SME needs.

*Employers' organizations*

28.

(i) The ILO, in particular through its Employers' Activities Programme, should assist in strengthening, or, where they do not already exist, in establishing, employers' organizations able to represent SMEs and their interests. SMEs should be encouraged to become active members of these organizations;

(ii) the ILO should assist employers' organizations in developing advisory, training and other services for SMEs. Technical experts employed by these organizations should be provided with adequate training;

(iii) employers' organizations should recognize the important role of workers' organizations in representing the legitimate interests of workers.

*Trade unions*

29. Recognizing the significance of the SME contribution towards national, social, economic and productivity gains, assistance to trade unions warrants ILO action by providing special training programmes for trade union officials relevant to the SME and informal sectors. Trade unions should also —

(i) play a role in the promotion of SMEs and in the informal sector; and

(ii) obtain necessary information on working and employment conditions in SMEs.

*Other non-governmental involvement*

30. The ILO should support the idea of using the services of NGOs, national and international, for promoting entrepreneurship and small enterprise creation, and assisting entrepreneurs, in particular in rural areas and the informal sector. Contacts with interested NGOs should be intensified and their training needs identified. The ILO can develop training programmes and packages for use by NGOs' staff, thus contributing to the improvement of standards in this assistance. Consultations and workshops for NGOs should be organized in collaboration with donor agencies that are keen to increase the NGOs' role in SME promotion.

*International institutional support*

31. Contacts with other organizations, international and national, including development banks and financing agencies, and training exchange programmes should be strengthened with a view to increasing the volume and improving the coordination and impact of assistance programmes for the SME sector. Coordination should concern not only resource allocation and the definition of sectoral and regional priorities, but also the policy approach taken and the intervention methods applied by specific programmes and projects, which should be closely connected with the economic and social development policies and plans of the countries concerned.

*Developmental activities*

*Training and education*

32.

(i) The ILO should encourage and support the development of training, advisory and extension services for SMEs and entrepreneurship development by providing policy guidelines, assisting in training needs assessment and programme design, training trainers and producing appropriate training materials. This assistance should cater for specific categories of people in the SME sector, such as would-be and new entrepreneurs, self-employed persons, SMEs facing expansion opportunities or SMEs in difficulties;

(ii) experience with successful training and assistance programmes such as *Improve Your Business* should be used for producing similar materials for specific client groups, including materials in local languages;

(iii) SME managers and entrepreneurs should be helped to learn from successful managers in both industrialized and developing countries through case materials, workshops, factory visits, study tours, business clinics, etc. Similar endeavours involving workers should be developed. Increased attention ought to be paid to new training technologies aimed at achieving a high benefit/cost ratio of training services;

(iv) using its experience and influence, the ILO should encourage member States. as well as technical and donor agencies active in the education sector, to re-examine the relevance of education to the needs of industrial and business practice. Major reforms may be necessary in order to prepare graduates for self-employment and business creation.

*Information and research on SMEs*

33.

(i) As SME development suffers from an acute shortage of information and decisions are often based on beliefs rather than hard data, the ILO should help member States to build up effective and reliable information services needed by entrepreneurs and SME managers as well as by decision-makers responsible for SME promotion. This information should cover issues such as investment, marketing and export opportunities, sources of technology and finance, training and advisory services available, as well as labour and social aspects;

(ii) the ILO should consider the feasibility of establishing a coordinated international information service on SMEs, using and supplementing the information services that may exist in some member States and in other international agencies;

(iii) in certain cases new research studies will need to be undertaken or encouraged by the ILO to obtain information on significant trends and on problems of SMEs requiring remedial action or special assistance.

*Technology for development*

34.

(i) Within its resources and technical possibilities, the ILO should expand its work on providing information on technologies of interest to SMEs in developing countries and help member States to devise policies that encourage local research, appropriate technological choices and adaptation of technologies to local conditions;

(ii) technology transfer between SMEs in various countries and other forms of technological cooperation, including their training and social implications, will also require increased ILO support.

*Marketing*

35.

(i) New forms of assistance to SMEs in marketing their products, including export marketing, should be given consideration in collaboration with other agencies such as the International Trade Centre. In many countries SMEs ought to be helped to become more export-oriented and meet necessary design, quality and cost standards;

(ii) legitimate subcontracting and other forms of cooperation between larger and smaller enterprises should be encouraged through training and information services.

*Finance*

36.

(i) The critical importance of finance to SME development calls for special ILO attention. Collaboration with funding and donor agencies should be enhanced. The ILO should try to influence the lending policies and procedures of financial and other institutions in order to help SMEs to obtain better access to credit;

(ii) training and advisory services ought to be provided in addition to credit and financial assistance. The ILO should pursue its efforts in training staff of development and commercial banks which are involved in lending to small firms, as well as in training aimed at improving the design of projects and the preparation of loan requests. Further training manuals on financial control and accounting in SMEs should be developed and disseminated;

(iii) the ILO should express to the World Bank and other international agencies responsible for economic and financial policies the urgent need for these agencies to examine the problem of the burden of foreign debt that weighs heavily on many developing countries

and should ask that these agencies consult the ILO on all matters relating to social and labour aspects of the problem, particularly those relating to SMEs.

*Labour and social aspects*

37.

(i) ILO programmes should give greater attention to conditions of work and employment as well as the social security of workers in SMEs, which have received little attention in past years. This should be remedied by studies, recommendations to member States, advisory services, organized exchange of experience and training and dissemination of information concerning essential labour and social aspects such as the application of international labour standards in the SME sector;

(ii) the promotion of labour legislation and inspection, health and safety and the abolition of child labour are also priority areas for ILO action;

(iii) the ILO should encourage assistance for workers in the case of termination of employment due to business failures, restructuring and relocation of SMEs.

*Sector-specific activities*

*Rural development*

38. Assistance with SME and entrepreneurship development in the rural sector will be a priority area of the ILO's action for many years. Actions and services suggested by these recommendations should therefore in many cases be oriented towards the rural sector. Appropriate training and development programmes should be applied to reach artisans and potential entrepreneurs in rural areas.

*Informal sector*

39.

(i) Based on objective studies of the informal sector's problems and potential in particular countries, ILO programmes should focus on assisting entrepreneurs and self-employed individuals in the informal sector through training, information, workshop facilities, technical advice and similar activity. The ILO also should ensure the protection of the legitimate rights of workers in this sector;

(ii) because of the nature and magnitude of the problems of the informal sector, the ILO should consider placing it as an agenda item of a future Conference.

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